SPECIAL TOPICS

Alternative Dispute Resolution

ADR or Else?

In last year's *Year in Review*,[1] the authors commented on an Air Force alternative dispute resolution (ADR) initiative that included the timely identification and resolution of issues in controversy as a consideration in contractor past performance evaluations.[2] Despite resistance from private contractors and attorneys, the Air Force officially revised its Contractor Performance Assessment Reporting System (CPARS) and incorporated this initiative into its December 2001 CPARS guide.[3] In May 2002, the Air Force revised the CPARS's coverage of ADR again, "to clarify [that the Air Force] encourage[s] timely resolution of issues, but [does] not mandate how an issue is resolved."[4]

The Air Force's most recent revision came on the heels of a directive from Angela Styles, Administrator of the Office of Federal Procurement Policy (OFPP). On 1 April 2002, Ms. Styles instructed all federal agencies that the "filing of protests, the filing of claims, or the use of Alternative Dispute Resolution, must not be considered by an agency in either past performance or source selection decisions."[5] While encouraging federal agencies to use ADR where appropriate, the OFPP directive states that "contractors should feel free to avail themselves of the rights provided them by law."[6] The OFFP directive also instructs procurement executives to emphasize to all agency acquisition personnel, but especially source selection officials, that: (1) "[c]ontractors may not be given 'downgraded' past performance evaluations . . . for filing protests and claims or deciding not to use ADR;" and (2) "[c]ontractors may not be given 'positive' past performance evaluations for refraining from filing claims or protests or for agreeing to use ADR."[7]

In February 2002, David Drabkin, Deputy Associate Administrator for the General Services Administration (GSA), had issued similar guidance in a policy letter applicable to all GSA-issued or administered contracts, including those of agencies that make use of GSA multiple award schedules and government-wide contracts.[8] Mr. Drabkin stated that a "contractor's judicious exercise of a process protection is not evidence of unreasonable or uncooperative behavior" and therefore, "absent a clear pattern of frivolous or bad faith exercise of such protections, you cannot downgrade a contractor's performance for filing a protest or claim, or declin[e] to participate in an ADR process."[9]

ADR and Schedule Disputes . . . It's Final

While the OFPP and the GSA frown upon contracting agencies evaluating contractors' past performance based on their (un)willingness to participate in ADR procedures, it is clear that agencies encourage the use of ADR in resolving disputes. In June 2002, a final rule announcement amended the Federal Acquisition Regulation (FAR) to incorporate policies for dispute resolution in federal schedule contracts.[10] The proposed rule stated that contracting officers should, when resolving disputes arising out of federal schedule contracts, "use the alternative dispute resolution (ADR) procedures, when appropriate."[11]

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1. Major John J. Siemietkowski et al., *Contract and Fiscal Law Developments of 2001—The Year in Review,* ARMY LAW., Jan./Feb. 2002, at 75 [hereinafter *2001 Year in Review*].

2. *See* Martha A. Matthews, *Air Force Revising CPARS to Urge Contractors to Resolve Disputes, Avoid Litigation*, 76 BNA FED. CONT. REP. 12 (Oct. 2, 2001).

3. *See Air Force Adds ADR Initiative to CPARS*, 44 GOV'T CONTRACTOR 2, ¶ 19(c) (Jan. 16, 2002).

4. U.S. DEP'T OF AIR FORCE, CONTRACTOR PERFORMANCE ASSESSMENT REPORTING SYSTEM (May 2002). More specifically, the newest CPARS guidance states that "ratings of how well the contractor worked with the government to identify and resolve issues should focus on the contractor's cooperation in identifying and resolving issues without regard to the means of resolution of the issue." *Id*. para. 7.2.4. It further states that "[c]ontracting agencies should not lower an offeror's past performance evaluation based solely on its having filed claims . . . or bid protests." *Id*.

5. Memorandum, Angela B. Styles, Administrator, Office of Federal Procurement Policy, to Senior Procurement Executives, subject: Protests, Claims, and Alternative Dispute Resolution (ADR) as Factors in Past Performance and Source Selection Decisions (Apr. 1, 2002) [hereinafter Past Performance Memo], *available at* http://www.acqnet.gov/notes; *see also* Martha A. Matthews, *OFPP: Protests, Claims, Use of ADR Can't Be Factors in Evaluation Source Selection*, 77 BNA FED. CONT. REP. 14 (Apr. 9, 2002); *Protests and Claims History Cannot Be Used to Downgrade Past Performance, OFPP Says*, 44 GOV'T CONTRACTOR 14, ¶ 138 (Apr. 10, 2002).

6. Past Performance Memo, *supra* note 5, para. 2.

7. *Id*.

8. *See* Martha A. Matthews, *GSA Policy Forbids Downgrading Contractor for Filing Claims, Refusing to Use ADR*, 77 BNA FED. CONT. REP. 10 (Mar. 12, 2002); *Exercise of Legal Rights May Not Affect Past Performance Evaluations, GSA Says*, 44 GOV'T CONTRACTOR 8, ¶ 83 (Feb. 27, 2002).

9. Matthews, *supra* note 8, at ¶ 83.

10. Federal Acquisition Regulation; Federal Supply Schedule Order Disputes and Incidental Items, 67 Fed. Reg. 43,514 (June 27, 2002) (codified at 48 C.F.R. § 8.405-7). The final rule became effective 29 July 2002. *Id.*

Based on public comments that the language used should be consistent with ADR policy statements found elsewhere in the FAR, the final rule revised the proposed language to reflect that parties should use ADR "to the maximum extent possible" and incorporated references to both FAR section 33.204 and FAR section 33.214.[12]

ADR Doesn't Get Agency Off the Hook for Costs

In *National Opinion Research Center—Costs*,[13] the General Accounting Office (GAO) held that when an agency takes corrective action pursuant to the GAO outcome-prediction ADR[14] and after filing its agency report, the agency will presumably be "on the hook" for the protestor's costs. The National Opinion Research Center (NORC) sought reimbursement of costs for filing and pursuing a protest challenging the award of a contract by the Department of Health and Human Services (HHS) to operate a patient safety research coordinating center. In its protest filing, the NORC argued that the agency's evaluation and source selection determination were improper.[15] After an outcome-prediction conference, the GAO attorney advised the parties that the protest was likely to be sustained based on a "clearly flawed" source selection decision.[16] In response, the HHS advised that it would take corrective action by arranging for a new source selection authority from outside the HHS to conduct a new source selection. Based on the proposed corrective action, the GAO dismissed the protest as academic.[17]

While the outcome prediction ADR successfully resolved the case, the NORC still sought reimbursement of its costs for filing and pursuing its protest. The HHS did not oppose reimbursement, but requested a formal recommendation from the GAO. The GAO started with the general rule that it will recommend agency reimbursement of costs when "we determine that the agency delayed taking corrective action in the face of a clearly meritorious protest, thereby causing protestors to expend unnecessary time and resources to make further use of the protest process in order to obtain relief."[18] In an outcome prediction ADR, the GAO noted, the assigned attorney informs the parties that the GAO is likely to sustain a protest "only if she or he has a high degree of confidence regarding the outcome."[19] The GAO attorney's "willingness to do so," concluded GAO, is an "indication that the protest is viewed as clearly meritorious, and satisfies the 'clearly meritorious' requirement for purposes of recommending reimbursement for protest costs."[20] The GAO concluded by stating that agency corrective action following outcome-prediction ADR and the filing of the agency report[21] presumptively satisfies the cost-reimbursement standard, absent contrary persuasive evidence.[22]

We're Unoffically on the ADR Bandwagon . . . but We'd Like to Make It Official

While the GAO regularly uses ADR to resolve bid protests efficiently and expeditiously, its Bid Protest Regulations[23] currently make no mention of these procedures. The GAO may

11. Federal Acquisition Regulation; Federal Supply Schedule Order Disputes and Incidental Items, 65 Fed. Reg. 79,702 (Dec. 19, 2000) (amending GENERAL SERVS. ADMIN. ET AL., FEDERAL ACQUISITION REG. 8.405-7(d) (Sept. 2001)).

12. 67 Fed. Reg. at 43,515. The language in FAR section 33.204 addresses the "government's policy to try to resolve all contractual issues in controversy by mutual agreement at the contracting officer's level." GENERAL SERVS. ADMIN. ET AL., FEDERAL ACQUISITION REG. 33.204 (July 2002). In section 33.214, the FAR provides additional and more specific guidance about ADR. *See id*. at 33.214.

13. Comp. Gen. B-289044.3, Mar. 6, 2002, 2002 CPD ¶ 55; *see also Corrective Action: Protestor Entitled to Costs Although Agency Action Followed GAO Outcome Prediction ADR*, FED. CONTRACTS DAILY, Mar. 25, 2002.

14. Under the GAO's outcome-prediction ADR procedures, the GAO attorney assigned to the protest convenes the parties and provides them with the attorney's belief of the likely outcome of the case, and the reasons for that belief. *National Opinion Research Center—Costs*, 2002 CPD ¶ 55, at 2 n.1. The GAO only uses outcome prediction when the assigned GAO attorney has a "high degree of confidence" in the outcome. *Id*. If the predicted losing party takes corrective action in response, the GAO closes the case without issuing a written decision. While the prediction reflects the belief of the assigned attorney, the opinion does not bind the GAO if it needs to issue a written decision later. *Id*.

15. *Id*. at 1.

16. *Id*. at 2. More specifically, while the agency evaluation committee recommended that the source selection authority (SSA) award to the NORC and supported that recommendation with a detailed rationale, the SSA made an award to Westat, Inc., based on an executive committee group recommendation that was not supported by contemporaneous documentation. *Id*.

17. *Id*.

18. *Id*. at 3.

19. *Id*.

20. *Id*.

21. The GAO noted that it generally considers agency corrective action unduly delayed when the action is taken after the due date for the agency report. *Id*. at 3 n.2.

22. *Id*. at 3.

soon fill this void by adding proposed language to its regulations reflecting the current practice of using ADR to resolve protest cases.[24] In response to the comments it received, the GAO has proposed incorporating a definition of ADR in a new paragraph (h), in section 21.0 of its Bid Protest Regulations.[25] The proposal also revises paragraph (e) of section 21.10 "to specifically provide that ADR is among the flexible alternative procedures GAO may use to promptly and fairly resolve a protest."[26] Major Huyser.

23. 5 C.F.R. pt. 21 (1996).

24. Advance Notice; General Accounting Office, Administrative Practice and Procedure, Bid Protest Regulations, Government Contract, 67 Fed. Reg. 8485 (proposed Feb. 25, 2002) (to be codified at 4 C.F.R. pt. 21).

25. Proposed Rules; General Accounting Office, Administrative Practice and Procedure, Bid Protest Regulations, Government Contracts, 67 Fed. Reg. 61,542 (proposed Oct. 1, 2002) (to be codified at 4 C.F.R. pt. 21). The broad definition states, "Alternative dispute resolution encompasses various means of resolving cases expeditiously, without a written decision, including techniques such as outcome prediction and negotiation assistance." *Id*. at 61,544.

26. *Id*. at 61,542.

Classified Contracting

Who Pays the Tab?

Department of Defense (DOD) readers who support classified programs face more complicated contracting issues because of security concerns. Contractors working in the secure contracting environment subject their employees to an extensive Defense Security Service (DSS) background investigation before they can receive the appropriate clearance to work on classified contracts. The DSS investigative process is lengthy and expensive, and the DOD has historically paid the cost of vetting contractor employees. The DOD Comptroller examined these costs and proposed that such costs were a potential fee-for-service candidate in Program Budget Decision (PBD) 434. Under PBD 434, the DSS would directly charge contractors for their personnel security clearance investigations.[1]

The Under Secretary of Defense for Acquisition, Technology and Logistics conducted a study analyzing PBD 434 and non-concurred in the proposed fee-for-service proposal.[2] In surveying its five largest defense contractors, the Under Secretary determined that the proposal would "simply shift the current costs of performing contractor security clearances, including overhead, general and administrative . . . , and profit/fee to DOD weapons systems, thereby increasing the costs of those weapons systems and increasing the Department's costs in total."[3] The projected costs of implementing PBD 434 would result in the DOD paying an additional thirty-four percent over the current costs for such clearances. Contractors would be able to charge the clearance costs directly to DOD customers as a cost of doing business. The DOD would draw such additional costs from program funds, thus eating into program budgets which may already be tight.[4]

The study also determined that charging contractors for security clearances would not reduce the number of contractor clearance requests. The study noted that competitive market pressures already provide an incentive to limit personnel costs, including clearance costs, to only those employees necessary to perform the contract. Moreover, because the DSS is the mandatory source for DOD contractor security clearances, contractors questioned the remedies available to them against the DSS "in the event of quality or timeliness problems under the proposed fee-for-service arrangement."[5]

As an alternative to PBD 434, the Comptroller proposed that the DSS "direct charge" the military departments for costs of security clearances for contractor personnel working on their contracts.[6] The military departments rejected this proposal for several reasons. First, the proposal would result in increased personnel costs "required to manage the submission and adjudication of contractor security clearances, with no accompanying expectation that it would lead to future reductions in the number of contractor security clearance requests."[7] Second, it would be "impossible for Government contract managers to determine which Military Department should bear fiscal responsibility for processing a particular security clearance in a situation where multiple DOD contracts are being performed simultaneously by the same contractor."[8]

FAR Changes

A new amendment to the Federal Acquisition Regulation (FAR) consolidates and clarifies definitions concerning classified contracting and provides guidance on disclosure of classified sealed bids.[9] The first change moved the definitions of "classified acquisition," "classified contract," and "classified information" from FAR section 4.401, dealing with safeguarding classified information within industry, to FAR section 2.101, the general definitions section. This change clarifies that the definitions applied to more than one FAR part. The second change involved rewriting FAR section 14.402-2. The new amendment revised the language stating that only properly

1. Memorandum, Under Secretary of Defense (Acquisition, Technology and Logistics), to Deputy Secretary of Defense, subject: Study for Program Budget Decision (PBD) 434, Defense Security Service (30 May 2002). The costs for contractor personnel security clearances are currently charged against a DOD-wide Operation and Maintenance (O&M) appropriation. *Id.*

2. Under Secretary of Defense (Acquisition, Technology & Logistics) Study for PBD 434, Defense Security Service (undated) (on file with author).

3. *Id.* at 1.

4. *Id.* In fiscal year 2002, the DOD projected costs of $91.2 million in Operation and Maintenance funds if the DOD paid directly for the clearances, and $122.2 million if the DOD used the proposed fee-for-service system. *Id.*

5. *Id.* Among the questions contractors asked were whether contractors could legitimately refuse to pay the DSS or take any legal action against it in such situations. *Id.*

6. *Id.* at 2.

7. *Id.*

8. *Id.*

9. FAC 01-04, FAR Case 2000-404, Definitions for Classified Acquisitions, 67 Fed. Reg. 6,113 (proposed Feb. 8, 2002). The final rule became effective 20 February 2002.

cleared bidders or their representatives may attend classified bid openings, and added language allowing the contracting officer to make classified bids available to such properly cleared bidders or representatives at a time after bid opening.[10] Colonel Kosarin.

10. *Id*.

Competitive Sourcing

Does competitive sourcing ever have an "off" year? The rules of competitive sourcing remain in constant flux because of the high stakes in jobs and dollars, and the broad initiative for practitioners in this field. The process of conducting public-private cost-comparison studies under *Office of Management and Budget* (*OMB*) *Circular A-76*[1] and the *Revised Supplemental Handbook* (*RSH*)[2] is certainly as much a political issue as a legal issue. Competitive sourcing continues to be a topic of important concern to many contract attorneys.

The Never-Ending Tale of Jones-Hill Joint Venture

Some cost-comparison studies never seem to end; instead, they go on like bad daytime soaps, providing an unending stream of drama and suspense, but no finality. One such example is *Jones/Hill Joint Venture*. At the time of writing of last year's *Year in Review*,[3] the GAO had decided the issue of Jones/Hill's entitlement to protest costs, including attorneys' fees, for an earlier protest in which the agency took corrective action.[4] The Navy then reviewed its original determination that it would be more economical to perform its own base operations, real property maintenance, and operations services for the Naval Air Station, Lemoore (NASL), California, using government employees rather than contracting with Jones/Hill for these services.[5] When the agency's review ended with the same cost-comparison determination, the *Jones/Hill Joint Venture* protest returned with a vengeance.[6]

Jones/Hill's protest raised several allegations, including some that it had raised in its original protest action.[7] The critical and novel issue, however, was Jones/Hill's contention that the agency's use of both a private-sector consultant and a Navy employee to prepare the solicitation's performance work statement (PWS) and to draft the in-house proposal constituted an impermissible conflict of interest. This occupied the bulk of the GAO's decision.

As one of the first steps in the NASL cost-comparison study process, the Navy organized a commercial activities (CA) team to plan the study.[8] Included among the CA team's functions was the development of the PWS, which represented the agency performance requirements that it required both the private sector and in-house proposals to meet. Several CA team members—including the CA team leader and employees of the consultant contractor—subsequently became members of the most efficient organization (MEO) team responsible for developing the in-house management plan. In its protest, Jones/Hill argued that the Navy employee and private-sector consultants who served in these multiple roles had a conflict of interest which violated applicable standards of conduct and gave the MEO team an unfair competitive advantage.[9] The GAO agreed.[10]

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1. U.S. Office of Mgmt. & Budget, Circular No. A-76, Performance of Commercial Activities (1999) [hereinafter OMB A-76].

2. U.S. Office of Mgmt. & Budget, Circular A-76, Revised Supplemental Handbook, Performance of Commercial Activities (1996) [hereinafter RSH].

3. *See* Major John J. Siemietkowski et al., *Contract and Fiscal Law Developments of 2001—The Year in Review*, Army Law., Jan./Feb. 2002, at 80 [hereinafter *2001 Year in Review*].

4. Jones/Hill Joint Venture—Costs, Comp. Gen. B-286194.3, Mar. 27, 2001, 2001 CPD ¶ 62. As part of its conclusion that Jones/Hill's initial protest was clearly meritorious, the GAO explained how agencies should conduct a competitive sourcing studies properly, at great length. *Id*. at 9-13.

5. *Id.* at 7. The agency had agreed that its corrective action would examine various strengths in Jones/Hill's proposal that had been identified but not considered, and that it would adjust its in-house plan as necessary to account for those strengths "that predict a higher quality performance (as opposed to 'strengths' such as a well-written proposal)." *Id.* at 7 (quoting the Agency's Post-ADR Comments, at 10). The agency also stated that it would adjust the in-house management plan as necessary and prepare a detailed written justification of its conclusion. *Id.*

6. Comp. Gen. B-286194.4, B-286194.5, B-286194.6, Dec. 5, 2001, 2001 CPD ¶ 194.

7. *Id*. at 6. Jones/Hill argued that: (1) the agency had unreasonably determined that the MEO could perform the work required with the number of personnel proposed in the in-house plan; (2) that the in-house management plan provided for the performance of certain tasks by individuals who were not part of the MEO; and (3) that the agency's determination that the MEO and Jones/Hill's proposal offered the same level of performance and performance quality was unreasonable. *Id*. The GAO decision sustained Jones/Hill's protest on these grounds. *Id*. at 18-19, 21.

8. *Id*. at 7. The CA team was comprised of Navy personnel assisted by a private consultant, E.L. Hamm, Inc. *Id.*

9. *Id.* at 8. The CA team leader, who participated in drafting and developing the PWS, became the MEO team leader. E.L. Hamm, considered a "co-producer" and "active coparticipant in the preparation of the PWS," became a "full participant" in the MEO team's development of the in-house proposal. *Id*.

10. *Id*. at 18-19.

In setting out the standards of conduct that apply to government business, the GAO noted that the Federal Acquisition Regulation (FAR) requires agencies to conduct such business in a manner above reproach.[11] While the FAR does not provide specific guidance regarding situations where job positions or relationships with particular government organizations create conflicts of interest for government employees, the GAO noted that FAR subpart 9.5 addressed analogous situations involving contractor organizations.[12] Here, the FAR broadly categorizes organizational conflicts of interest into three groups: "unequal access to information" cases,[13] "biased ground rules" cases,[14] and "impaired objectivity" cases.[15] The GAO found that, "given the use of the competitive system in *Circular A-76* studies and the MEO team's status as essentially a competitor in the study," the FAR provisions at subpart 9.5 served as useful guidance in determining the presence of conflicts of interest.[16]

Because the facts were not in dispute, the GAO also determined that the record was "consistent with the circumstances attendant to both 'unequal access to information' and 'biased ground rules' conflicts of interest."[17] Finding no reason to treat government employee conflicts of interest differently than contractor-employee conflicts of interest, the GAO concluded that "the appearance of impropriety resulting from the conflicts of interest here has tainted the integrity of the process,"[18] and sustained this part of Jones/Hill's protest. Regarding the resulting remedy, the GAO recommended that the agency essentially start over—that it should issue a new PWS, drafted by individuals who would not subsequently draft the in-house management plan; prepare a new in-house management plan; solicit new proposals for private-sector offerors; and conduct a new cost comparison.[19]

Jones/Hill Joint Venture—*One More Time?*

The impact of the *Jones/Hill* decision, including the GAO's recommendation for an appropriate remedy, stood to affect not only the Navy's cost-comparison study at NASL, but as many as 160 ongoing agency competitive sourcing studies. The Navy, therefore, requested reconsideration of the GAO's decision to the extent that it concluded that a conflict of interest existed.[20] The GAO affirmed its decision, but it modified the recommended corrective action to apply the conflict of interest portion of the decision prospectively only.[21]

Without disputing the underlying facts—that a government employee and consultant-contractor employees developed both the PWS and the in-house management plan—the agency set forth several arguments challenging the GAO's conclusion. The Navy first challenged the GAO's characterization of the MEO team as "essentially a competitor."[22] The GAO found

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11. More specifically, the FAR provides:

> Government business shall be conducted in a manner above reproach and, except as authorized by statute or regulation, with complete impartiality and with preferential treatment for none. Transactions relating to the expenditure of public funds require the highest degree of public trust and an impeccable standard of conduct. The general rule is to avoid strictly any conflict of interest or even the appearance of a conflict of interest in Government-contractor relationships.

GENERAL SERVS. ADMIN. ET AL., FEDERAL ACQUISITIONS REG. 3.101-1 (July 2002) [hereinafter FAR].

12. Jones/Hill Joint Venture—Costs, Comp. Gen. B-286194.3, Mar. 27, 2001, 2001 CPD ¶ 62, at 9 (citing DZS/Baker LLC; Morrison Knudsen Corp., Comp. Gen. B-281224, Jan. 12, 1999, 99-1 CPD ¶ 19, at 4; Battelle Memorial Inst., Comp. Gen. B-278673, Feb. 27, 1998, 98-1 CPD ¶ 107, at 6-7).

13. *Id*. at 10. Such cases include situations in which a firm has access to non-public information as part of its performance of a government contract, and where that information may provide the firm an unfair competitive advantage in a later competition for a government contract. *Id*. (citing FAR, *supra* note 11, at 9.505-4; Aetna Gov't Health Plans, Inc.; Foundation Health Fed. Servs., Inc., Comp. Gen. B-254397.15, July 27, 1995, 95-2 CPD ¶ 129, at 12).

14. *Id*. Such cases include situations in which a firm, as part of its performance of a government contract, has somehow set the ground rules for the competition for another government contract, for example, by writing the statement of work or the specifications. *Id*. (citing FAR, *supra* note 11, at 9.505-1, 2; *Aetna Gov't Health Plans*, 95-2 CPD ¶ 129, at 13).

15. *Id*. Such cases include situations where a firm's work under one government contract could require it to evaluate itself or a related entity, either through an assessment of performance under another contract or an evaluation of proposals. *Id*. (citing FAR, *supra* note 11, at 9.505-3; *Aetna Gov't Health Plans*, 95-2 CPD ¶ 129, at 13).

16. *Id*. at 11.

17. *Id*. at 10.

18. *Id*. at 14.

19. *Id*. at 21-22.

20. Department of the Navy—Reconsideration, Comp. Gen. B-286194.7, May 29, 2002, 2002 CPD ¶ 76. The Navy did not challenge the other bases upon which the GAO had sustained the protest. *Id*. at 4-5.

21. *Id*. at 12.

that, notwithstanding the fact that the MEO team was not legally an offeror, the MEO team members functioned, and viewed themselves, as competitors.[23] The Navy also argued that in-house teams were still factually distinguishable from private-sector competitors, leaving an adequate basis "to exempt MEO teams from application of the conflict of interest rules generally applicable to private-sector competitors."[24] The GAO did not dispute the Navy's factual observations, but it rejected the agency's conclusion that the nature and status of the MEO team justified exempting that team from the conflict of interest limitations generally applied to private-sector competitors.[25]

The Navy also challenged the GAO's application of FAR subpart 9.5 to the *OMB Circular A-76* process. In response, the GAO stated that in complying with the obligatory conflict of interest requirements of FAR subpart 3.1, "it is not reasonable for an agency to ignore the instruction and guidance provided by FAR subpart 9.5."[26] The GAO also rejected the Navy's argument that Jones/Hill had failed to demonstrate any prejudice, holding that "where a protest establishes facts that constitute a conflict of interest or apparent conflict of interest, [the GAO] will presume prejudice unless the record affirmatively demonstrates its absence."[27]

Lastly, the GAO examined the agency's request that the GAO modify the recommended corrective action. The GAO analyzed which parties its original corrective action would help or harm, and concluded,

> [W]e believe that the integrity of the decision-making process in A-76 cost studies should be above reproach. Nonetheless, just as our decision reflected the reality that A-76 studies are essentially public/private competitions, we believe it important to recognize the practical realities supporting the agencies' request for prospective application of the conflict of interest portion of our decision. The fact is that disruption or cancellation of large numbers of studies will not serve the private-sector firms who would presumably be disadvantaged by the conflicts, nor the agencies endeavoring to conduct the studies, nor the viability of the A-76 process overall.[28]

Accordingly, the GAO modified its recommended corrective action so that it applied prospectively only.[29] It will not be necessary, therefore, for the Navy or any other federal agency to unravel all ongoing cost-comparison studies when the same employees prepared both the PWS and the in-house proposal.[30]

A New Twist in A-76 Cost Comparisons

In *Sodexho Management Inc.*,[31] the GAO confronted another novel issue for the competitive sourcing process—the reliance on nonappropriated fund instrumentality (NAFI) employees as part of an MEO's proposed staffing solution.[32]

The Navy began a commercial activity study for the performance of various community support services at the Pensacola Naval Regional Complex in Pensacola, Florida.[33] The agency received proposals from two private sector offerors, and determined that Sodexho's proposal represented the best value to the government. As part of the commercial activity study, a cost-analysis team (MEO team) of Navy personnel and contractor

22. *Id*. at 4.

23. *Id*. at 4-5.

24. *Id*. at 6.

25. *Id*. at 6-7.

26. *Id*. at 9.

27. *Id*. at 12.

28. *Id.* at 13. The Office of the Under Secretary of Defense, the Army, and the Defense Logistics Agency also joined with the Navy in asserting that the GAO's recommended corrective action would have a serious negative impact on multiple ongoing A-76 studies. *Id.*

29. *Id*. at 14 n.18. The GAO established that the effective date for the prospective application of the *Jones/Hill* decision was the date the redacted version of the decision was released to the public—10 December 2001. *Id*.

30. *Id*. at 14-15. The GAO decision also provides agencies with detailed guidance for its implementation with regard to ongoing cost comparison studies. *Id.*

31. Comp. Gen. B-289605.2, July 5, 2002, 2002 CPD ¶ 111.

32. *Id.* at 7. "NAFIs are not federal agencies or government corporations, and they are not typical private or commercial enterprises, although they may operate on a for-profit basis. Instead, they are 'a special breed of federal instrumentality which cannot be fully analogized to the typical federal agency supported by federal funds.'" *Id.* (quoting Cosme Nieves v. Deshler, 786 F.2d 445, 448 (1st Cir. 1986)). *See also* General Acct. Off., Principles of Appropriations Law vol. IV, GAO-01-179SP, ch. 17, pt. C (2001) (examining the history and legal status of NAFIs in detail). Employees of NAFIs receive lower wage rates and benefits levels than federal employees within the civil service. *Sodexho Mgmt. Inc.*, 2002 CPD ¶ 111, at 11.

personnel developed the government's in-house management plan and MEO. In the subsequent cost comparison, the agency determined that Sodexho's adjusted price for performing the required services was $82,641,457, while the adjusted in-house plan's cost would be $56,460,369, a difference of more than $26 million.[34] This resulted in a tentative decision to perform the requirements in-house. Sodexho protested to the GAO, arguing that the Navy's decision process was flawed and unfair because the cost comparison was based on an MEO that proposed to perform the PWS requirements using NAFI employees for eighty-two percent of its in-house workforce.[35]

Contrary to the protester's arguments, the GAO first determined that neither federal law nor the *RSH* necessarily barred the use of NAFI employees in an MEO.[36] The GAO thus did not find that the inclusion of NAFI employees in the MEO violated the procedures of *OMB Circular A-76*.[37] The GAO concluded, however, that the wholesale use of NAFI employees in the circumstances of this case resulted in an unfair competition. "In conducting an A-76 competition, as in any competition for a federal contract, an agency must provide private offerors with sufficient information to allow an intelligent competition on an equal basis."[38]

Here, neither the A-76 guidance nor the solicitation permitted Sodexho to reasonably anticipate the extensive use of NAFI employees. Accordingly, the GAO sustained the protest, holding that "fundamental fairness" dictated that the Navy should have provided commercial offerors adequate notice of the intended heavy reliance on the use of NAFI employees. Because the GAO did not find it unlawful for the Navy to rely so heavily on NAFI employees, and because Sodexho indicated that it would not have competed if the Navy had given it notice in this regard, the GAO had no basis to conclude that Sodexho would participate in a recompetition. As a result, the GAO recommended the Navy merely reimburse Sodexho for its bid proposal and protest costs.[39]

Government Employees and Judicial Standing—Again

In last year's *Year in Review*, the authors questioned whether the CAFC had finally ended the debate on whether government

33. *Sodexho Mgmt. Inc*., 2002 CPD ¶ 111, at 2. The solicitation divided the required support services into separate "annexes," including Navy family housing, bachelor housing, morale, welfare, and recreation (MWR) activities, and public affairs functions. *Id*.

34. *Id*. at 5. An administrative appeal by Sodexho resulted in a revised cost comparison; the new comparison study found that the difference between contract performance and in-house performance was $24,653,748. *Id.*

35. *Id*. at 26-28. The GAO considered and rejected Sodexho's other protest issues—that the MEO failed to meet numerous PWS requirements, that the independent review official's certification of the MEO was inadequately documented, and that the agency improperly failed to adjust the in-house offer to a level of performance and performance quality equal to that offered by Sodexho. *Id*.

36. *Id*. at 15.

> [W]hile we agree that the RSH's procedures and standard cost factors were designed for civil service employees under the GS [general schedule] and FWS [federal wage system] wage systems, we cannot conclude that the RSH's specification of these two wage systems, and no others, must be read to prohibit the use of NAFI employees in an MEO.

Id.

37. *Id*. at 17. The GAO did note, however, that the reliance on NAFI employees "raises significant policy concerns, which are to be resolved, not by our Office's bid protest function, but by the executive branch, and by OMB, in particular, as the agency responsible for the [A-76] Circular." *Id.*

38. *Id.* at 18 (citing Ameriko Maint. Co., Comp. Gen. B-243728, Aug. 23, 1991, 91-2 CPD ¶ 191, at 3; Draeger Safety, Inc., Comp. Gen. B-285366, B-285366.2, Aug. 23, 2000, 2000 CPD ¶ 139, at 4).

39. *Id.* at 29. One could argue that the GAO reached the wrong result in this protest. *Sodexho* clearly turns not on the use of NAFI employees per se—which the GAO did not find improper—but instead on the degree of reliance on NAFI employees without notifying commercial offerors of this first, which the GAO found unfair. What the GAO failed to take into account, however, was *who* was relying primarily upon NAFI employees and *who* had an obligation to provide offerors with sufficient information to allow an intelligent competition on an equal basis. Because the two were not the same entity here, the argument that the agency failed in its duty to provide Sodexho with adequate information is questionable. At the beginning of the decision, the GAO recognized that it was the MEO team that developed the in-house proposal and that it was the MEO's use of NAFI employees that Sodexho was challenging. *Id*. at 4, 6. The GAO blurred this critical distinction, however, when it found that it was the Navy's wholesale use of NAFI employees that was unfair, and that it was the Navy's intent to use NAFI employees for the great majority of the in-house work force. *Id*. at 18, 20-21. Because it was the MEO team that decided on the degree of reliance on NAFI employees for the in-house proposal, and because the GAO has determined that the MEO team is "essentially a competitor" in the competitive sourcing process, it is uncertain why the agency had any obligation to disclose this information to private sector offerors. Surprisingly, the Navy—the very agency affected by *Jones/Hill* and the decision that the MEO team was "essentially a competitor"—did not present this argument to the GAO. Because the GAO determined that the use of NAFI employees was not improper, the MEO team's decision to rely on such employees was essentially a fair competitive advantage of the in-house offeror. *OMB Circular A-76* requires that the agency "provide a level playing field between public and private offerors to a competition." *Id.* at 18 (quoting RSH, *supra* note 2, at iii). Neither *OMB Circular A-76* nor any other procurement statute or regulation requires or permits the agency to level the fair competitive advantages of the various offerors to a competition. *See* OMB A-76, *supra* note 1. The agency did not deprive Sodexho of the ability to make an intelligent business judgment about whether to compete; a fellow competitor, albeit a public one, deprived Sodexho the ability to make an *error-proof* business judgment about whether to compete. It is difficult to understand the legal and equitable rationales for sustaining this protest.

employees have standing to challenge *OMB Circular A-76* decisions.[40] As events of the past year have shown, this is an issue that will not go away.

Last year, in *American Federation of Government Employees, Local 1482 v. United States*,[41] the Federal Circuit affirmed the COFC decision that federal employees are not interested parties and do not have standing to challenge cost-comparison studies or the contract award decisions that resulting from them.[42] The employees and unions, having nothing to lose but their jobs, filed a petition for writ of certiorari with the Supreme Court. On 22 January 2002, the Supreme Court denied the petition without comment.[43]

While the Supreme Court decision closes the door on unions' and federal employees' attempts to challenge cost-comparison studies in court, other events of the past year indicate that legislation may result in same changes these parties sought in court. One congressman's attempt to sue personally on behalf of federal employees adversely affected by a cost-comparison study may be admirable (as well as the ultimate example of constituent services), but it did not prove successful. In *Kucinich v. Defense Finance & Accounting Service*,[44] Rep. Dennis J. Kucinich (D—Ohio) sued to challenge a Defense Finance & Accounting Service (DFAS) cost-comparison decision under *OMB Circular A-76*. Kucinich alleged that DFAS's cost comparison violated *OMB Circular A-76* and the Federal Activities Inventory Reform (FAIR) Act,[45] as well as the constitutional rights of due process, equal protection, and free speech of the affected federal employees, who unlike private sector offerors, were prohibited from seeking judicial review of the cost-comparison decision.[46]

Applying the Supreme Court precedent in *Raines v. Byrd*,[47] the district court determined that Kucinich was bringing the suit not to remedy the deprivation of a personal entitlement, but as a representative of his constituents (i.e., to vindicate an institutional injury).[48] As such, the court determined that Kucinich had "no more standing to sue than does any other taxpayer in the affected region," and his only remedy was "the one he possesses by virtue of his position as an elected official, that is, to convince his colleagues to amend the statutes regulating government contracts and forbidding federal court challenges by affected employees and unions."[49] Having concluded that Kucinich lacked standing, the court dismissed the case sua sponte for lack of jurisdiction.[50]

Sometimes You Can't Please Anyone

In a number of cost-comparison studies, in response to the myriad of issues raised, the agencies decided that the best thing to do was to cancel the solicitations. While "throwing in the towel" and starting over may have been prudent, such actions did not necessarily make everyone happy, and often resulted in protests.

In *IT Corp.*,[51] the GAO faced a protest objecting to the cancellation of a solicitation after the agency announced that it intended to award to the protester. The Navy had issued the

40. *2001 Year in Review*, *supra* note 3, at 82.

41. 258 F.3d 1294 (Fed. Cir. 2001).

42. *Id*. at 1299-1302. Although it affirmed the COFC's decision, the CAFC did so on different grounds. Unlike the trial court, the federal circuit applied the Competition in Contracting Act (CICA) jurisdictional standard, and found that neither the union nor the federal employees were actual or prospective offerors or bidders. *Id*. Similarly, the GAO has applied the same CICA jurisdictional standard and also determined that federal employees and their unions lack standing to protest adverse cost comparison study determinations. Am. Fed'n of Gov't Employees, Comp. Gen. B-282904.2, June 7, 2000, 2000 CPD ¶ 87.

43. Am. Fed'n of Gov't Employees v. United States, 258 F.3d 1294 (Fed. Cir. 2001), *cert. denied*, 534 U.S. 1113 (2002).

44. 183 F. Supp. 2d 1005 (N.D. Ohio 2002).

45. 10 U.S.C. § 2464 (2000); 31 U.S.C. § 501 (2000).

46. *Kucinich*, 183 F. Supp. 2d at 1006-07.

47. 521 U.S. 811, 819-20 (1997).

48. *Kucinich*, 183 F. Supp. 2d at 1011. The court succinctly noted the fundamental concern with representational capacity standing: "Kucinich, a member of Congress, asks this Court to invalidate the actions of an agency duly given the authority to take such actions by Kucinich's peers in Congress and to declare unconstitutional certain procedural provisions that forbid the employees or their union from bringing a suit like this themselves." *Id.*

49. *Id.* at 1011-12. While the court expressed sympathy for Kucinich's claim that federal employees had fewer available remedies than similarly situated private-sector offerors, the court stated that "unfortunately, it is not this Court whom Kucinich must persuade, but his peers in Congress. Congress and duly appointed administrative bodies have determined that aggrieved employees cannot bring their claims to this Court, and the Constitution does not allow Representative Kucinich to raise the claims for them." *Id.* at 1012.

50. *Id*. at 1012.

51. Comp. Gen. B-289517.3, July 10, 2002, 2002 CPD ¶ 123.

solicitation as part of a cost-comparison study, under *OMB Circular A-76*, for base operation support services at the Marine Corps Base, Camp Pendleton, California. After selecting IT as the best value private-sector offeror, and determining that its proposal represented a significant cost savings in comparison to the government's in-house management plan for an MEO, the Navy awarded to IT. This decision resulted in the protest by another private-sector offeror, Del-Jen, Inc., which objected to the agency evaluation of proposals. In response to Del-Jen's protest, the Navy took corrective action and cancelled the solicitation. IT then protested the solicitation cancellation to GAO.[52]

The GAO held that in a negotiated procurement, an agency has broad authority to decide whether to cancel a solicitation; there need only be a reasonable basis for the cancellation. This authority extends to the cancellation of solicitations used to conduct A-76 cost comparisons. So long as an agency has a reasonable basis to exercise this authority, it may cancel a solicitation regardless of when the information precipitating the cancellation surfaces.[53] Here, the GAO agreed with the Navy that the solicitation was deficient because it did not adequately identify all of the required work and contained incomplete and misleading historical workload information. These defects resulted in an unfair competition and even caused at least one potential offeror not to submit a proposal. The GAO thus concluded that the Navy's decision to cancel the solicitation and resolicit proposals was reasonable.[54]

In *Imaging Systems Technology* (*IST*),[55] the GAO revisited a protest challenging an agency cost-comparison decision as violative of federal statute; this time, the GAO denied the protest. As last year's *Year in Review* reported,[56] the Air Force had originally issued a solicitation in 1999 to acquire logistics support services for the programmable indicator data processor (PIDP) air traffic control and landing system. IST protested after the Air Force cancelled the original RFP, after deciding to assign the PIDP support function work to government employees as "other duties as assigned."[57] The GAO found that because the Air Force had failed to comply with 10 U.S.C. § 2462,[58] the agency's decision to cancel the solicitation lacked a reasonable basis.[59] The Air Force then prepared a second solicitation in 2001 that reflected the agency's revised views regarding its requirements. When the Air Force again determined that the cost of in-house performance would be lower than contractor performance, IST again protested.[60]

IST asserted that unlike its proposal, the in-house proposal planned performance using only technicians and did not include engineers. The GAO determined, however, that there was nothing on the face of the revised solicitation expressly stating that engineer or engineering services were required, and the personnel skill level descriptions and other changes from an earlier solicitation suggested that the solicitation did not require engineering services. Having concluded that IST had misread the solicitation, and had thus proposed higher-cost staffing than was necessary to perform the work, the GAO found no basis to sustain the protest.[61]

The Commercial Activities Panel Report

Last year's *Year in Review* reported that Section 832 of the FY 2001 National Defense Authorization Act directed the Comptroller General to convene a panel of experts to study federal outsourcing policy and report to Congress by 1 May 2002, with recommendations for legislative and policy changes.[62] On 30 April 2002, the Commercial Activities Panel met its deadline and issued its lengthy and long-awaited report, *Improving the Sourcing Decisions of the Government*.[63]

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52. *Id.* at 2. Del-Jen cited the unusually low price of IT's proposal as evidence for its claim that the agency's technical and price evaluations were inadequate and unreasonable. The proposed corrective action included a review of the evaluations, as well as a review of the adequacy of the PWS included within the solicitation. The agency's corrective action rendered Del-Jen's protest academic. *Id*.

53. *Id*. at 3 (citing Rice Servs., Ltd., Comp. Gen. B-284997.5, Mar. 12, 2002, 2002 CPD ¶ 59, at 4; Lackland 21st Century Servs. Consol., Comp. Gen. B-285938.7, B-285938.8, Dec. 4, 2001, 2001 CPD ¶ 197, at 5).

54. *Id*. at 4.

55. Comp. Gen. B-289262, Feb. 1, 2002, 2002 CPD ¶ 26.

56. *2001 Year in Review*, *supra* note 3, at 79.

57. Imaging Sys. Tech., Comp. Gen. B-283817.3, Dec. 19, 2000, 2001 CPD ¶ 2.

58. *Id*. at 6-7; *see* 10 U.S.C. § 2462 (2000). The statute requires that Department of Defense (DOD) agencies acquire goods or services from private sector offerors when doing so is cheaper than in-house government performance. In making such a cost comparison determination, the statute—similar to *OMB Circular A-76*—also requires agencies to ensure that all costs considered are realistic and fair. *Id*.

59. *Imaging Sys. Tech.*, 2001 CPD ¶ 2, at 4-7.

60. *Id*. at 26. The revised RFP contemplated that "either the award of a contract to the lowest priced, technically acceptable offeror or, if the government cost estimate showed that the requirements could be performed in-house for a lower cost, cancellation of the solicitation." *Id.* at 2 (citing 10 U.S.C. § 2562).

61. *Id*. at 5.

After establishing its organizational framework,[64] the panel unanimously developed a set of ten principles that it believed should guide competitive sourcing policy.[65] Using these principles, the Panel then assessed the strengths and weaknesses of the current A-76 process and subsequently adopted specific recommendations for improvement.[66] The Panel found that the current A-76 process "may no longer be an effective tool for conducting competitions to identify the most efficient and effective service provider."[67] By contrast, the Panel observed that for private-private competitions, the government already had "an established mechanism that has been shown to work as a means to identify high-value service providers: the negotiated procurement process of the Federal Acquisition Regulation."[68]

Thus, instead of attempting to revise the current A-76 process dramatically, the panel recommended replacing A-76 with a FAR-based approach, modified as necessary to accommodate public-private competitions. Under such an "integrated competition process,"[69] the public sector would have the same basic rights and responsibilities as the private sector, including equivalent evaluation criteria, accountability for performance, and the right to protest. The public sector would also be able to submit proposals in response to a broad range of government solicitations, including new work and work that agencies currently contract to the private sector.[70]

Because implementation and development of an integrated FAR-type process would require some time, and because current competitive sourcing studies are expected to continue, the panel also recommended that "some modifications to the existing [A-76] process can and should be made."[71] These changes would, among other things, strengthen conflict of interest rules, improve auditing and cost accounting, and provide for the

62. *2001 Year in Review*, *supra* note 3, at 84 (citing Pub. L. No. 106-398, § 832, 114 Stat. 1654, 1654A-221 (2000)). "Panel membership includes a wide spectrum of organizations affected by outsourcing policy, including representatives from federal employee labor unions, government contractors, the DOD and the OMB, as well as four at-large members." *Id.*

63. Gen. Acct. Off., Commercial Activities Panel, Improving the Sourcing Decisions of the Government (2002).

64. *Id*. at 32. At its organizational meeting, the panel

> adopted a mission statement that stressed the need to balance the diverse and frequently divergent interests of the various constituencies represented. The mission of the Panel was to devise a set of recommendations that would improve the current [competitive] sourcing framework and process so that they reflect a balance among taxpayer interests, government needs, employee rights, and contractor concerns.

Id.

65. The Panel's competitive sourcing principles were stated as follows:

> 1. Support agency missions, goals, and objectives.
> 2. Be consistent with human capital practices designed to attract, motivate, retain, and reward a high-performing federal work force.
> 3. Recognize that inherently governmental and certain other functions should be performed by federal workers.
> 4. Create incentives and processes to foster high-performing, efficient and effective organizations throughout the federal government.
> 5. Be based on a clear, transparent, and consistently applied process.
> 6. Avoid arbitrary full-time equivalent (FTE) or other arbitrary numerical goals.
> 7. Establish a process that, for activities that may be performed by either the public or the private sector, would permit public and private sources to participate in competitions for work currently performed in-house, work currently contracted to the private sector, and new work, consistent with these guiding principles.
> 8. Ensure that, when competitions are held, they are conducted as fairly, effectively, and efficiently as possible.
> 9. Ensure that competitions involve a process that considers both quality and cost factors.
> 10. Provide for accountability in connection with all sourcing decisions.

Id. at 33-36.

66. *Id*. at 5, 49. The panel adopted the recommendations by a two-thirds super-majority. *Id*.

67. *Id*. at 10. Noting that the original purpose of the A-76 process was to determine the "low-cost provider of a defined set of services," the panel observed that the federal procurement system has changed in the decades since the OMB first issued *Circular A-76* and has recognized that a "cost-only focus does not necessarily deliver the best quality or performance for the government." *Id.* The panel further stated that the A-76 process "has not worked well as the basis for competitions that seek to identify the best provider in terms of quality, innovation, flexibility, and reliability," and has become "an anomaly in the federal procurement process" and inconsistent with the panel's recommended principles. *Id.*

68. *Id.*

69. *Id.* "The Panel believes that in order to promote a more level playing field on which to conduct public-private competitions, the government needs to shift, as rapidly as possible, to a FAR-type process under which all parties compete under the same set of rules." *Id.*

70. *Id*. at 11.

71. *Id*.

establishment of "binding performance agreements" for successful MEOs.[72] Interestingly, the establishment of an MEO binding performance agreement, though not a contract, may constitute an "offer" in some cases, thereby giving its "offeror" legal standing under the CICA. Because the panel specifically found that federal employees should have standing to file protests against the conduct of public-private competitions,[73] the existence of binding performance agreements appears to be an expedient means—that is, one that does not require legislation—to achieve this end. Lieutenant Colonel Chiarella and Major Huyser.

72. *Id.* at 11, 52.

73. *Id.* at 9. ("Fairness requires that competing parties, both public and private, or their representatives, receive comparable treatment throughout the competition regarding, for example, . . . legal standing to challenge the way a competition has been conducted at all appropriate forums, including the General Accounting Office (GAO) and the United States Court of Federal Claims.").

Privatization

Nice Job, DOD, . . . but There Is Still a Long Way to Go

In a report to the Subcommittee on Military Construction of the House Committee on Appropriations, the General Accounting Office (GAO) reported that the Department of Defense (DOD) had achieved key financial goals for its Military Housing Privatization Initiative (MHPI).[1] The report recommended, however, that the DOD better define and assess its military housing needs, improve its life-cycle costs analysis, and make contractual and oversight changes to increase government protections in the housing privatization program.[2]

The GAO noted in its report that while implementation of the MHPI began slowly, the DOD has "picked up the pace" and has made the initiative the "primary means" for meeting a revised DOD goal of "eliminating inadequate housing by 2007, instead of the original goal of 2010."[3] Reviewing the first ten housing privatization projects within the DOD, the GAO reported that the DOD had exceeded its goal for leveraging government funds. The report found that "by investing about $185 million in the [ten] projects, DOD should obtain housing improvements that would have required about $1.19 billion in military construction funds" using conventional military construction funding procedures.[4] The GAO, based on DOD guidance, also estimated that the life-cycle costs of each of the first ten projects would "most likely" be less than the traditional military construction alternative.[5] The GAO cautioned, however, that these estimates were not necessarily reliable because of weaknesses in the methodology of the DOD's guidance for calculating such costs.[6]

While (or perhaps because) the pace of housing privatization has increased, the GAO remained critical of the DOD's inability to develop processes to determine housing needs consistently and accurately and to determine whether the local community is able to meet those needs at each installation.[7] Citing previous reports that have highlighted the same concern,[8] the GAO simply stated that the "DOD has failed to fix this longstanding problem."[9]

Finally, while noting that the DOD had included some contract safeguards to protect the government's long-term interests, the GAO recommended further improvements. First, the GAO found that the DOD could further protect the government with contract provisions for unexpected events. For instance, private developers received a significant increase in profits because their contracts did not adequately address increases in service member housing allowances.[10] Similarly, the DOD apparently had limited oversight of major reinvestment spending decisions. In all the privatization projects except one, the contract with the private developer included provisions "designed to capture at least a portion of any unanticipated rental revenues" and to accumulate these funds in project reinvestment accounts for future renovations, maintenance, and improvements.[11] Typically, installation officials and private developers decide how to use such funds jointly, with remaining amounts returning to the DOD for use on other privatization projects. The GAO questioned whether the service headquarters and the Office of the Secretary of Defense had adequate oversight over these spending decisions to ensure that such funds are not used unnecessarily.[12]

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1. GEN. ACCT. OFF., REP. NO. GAO-02-624, *Military Housing: Management Improvement Needed as Pace of Privatization Quickens* (June 2002) [hereinafter GAO-02-624]. The National Defense Authorization Act for Fiscal Year 1996, Pub. L. No. 104-106, § 2801(a)(1), 110 Stat. 186, 547 (1995), granted the DOD temporary authority to provide direct loans, loan guarantees, and other financial incentives to encourage private developers to renovate, manage, and maintain existing military housing units, as well as to construct, manage, and maintain new military housing units. Congress extended this authority through 31 December 2012 in last year's Authorization Act. National Defense Authorization Act for Fiscal Year 2002, Pub. L. No. 107-107, § 2805, 115 Stat. 1012, 1306 (2001) (amending 10 U.S.C. § 2885).

2. GAO-02-624, *supra* note 1, at 2-4.

3. *Id*. at 5.

4. *Id*. at 3.

5. *Id*. at 15.

6. *Id*. at 14-15. After adjusting the DOD's methodology and re-computing the data, the GAO estimated that "privatization would likely cost less than military construction in seven of the ten projects and cost more in the other three." *Id.* at 15.

7. *Id*. at 7-8.

8. *Id.* at 6 (citing GEN. ACCT. OFF., REP. NO. GAO-01-889, *Military Housing: DOD Needs to Address Long-Standing Requirements Determination* (Aug. 3, 2001)).

9. *Id*. at 7.

10. *Id*. at 21.

11. *Id*. at 22.

12. *Id*. at 23-24.

A Slower Pace for Utilities Privatization . . . the DOD Revises Its Goal

The pace of the DOD's utilities privatization program has been slower than it has been for housing. In 1998, *Defense Reform Initiative Directive (DRID) 49—Privatizing Utility Systems* (*DRID 49*) established a DOD goal of privatizing all DOD utility systems by 30 September 2003, except for those systems needed for unique security reasons, or when privatization is not economical.[13] On 9 October 2002, the DOD revised its goal and replaced *DRID 49* with its *Revised Guidance Memorandum*.[14] The revised goal establishes 30 September 2005 as the date by which "Defense Components shall complete a privatization evaluation of each utility system at every Active, Reserve, and National Guard installation, within the United States and overseas, that is not designated for closure under a base closure law."[15]

In addition to revising the milestones for utilities privatization, the *Revised Guidance Memorandum* provides updated instructions on "conducting the economic analysis, protecting the government's interests, making a determination to privatize, and conforming with state laws and regulations."[16] Among its several updates, the *Revised Guidance Memorandum* addresses the DOD's position concerning the applicability of state utility laws and regulations to the acquisition and conveyance of the government's utility systems.[17] The updates also include discussion of the recent class deviation from the cost principle at Federal Acquisition Regulation (FAR) section 31.205-20,[18] authorized by the DOD "for utilities privatization contracts under which previously government-owned utility systems are *conveyed* by a Military Department or Defense Agency to a contractor."[19] Finally, the new guidance specifically allows the service secretaries to include reversionary clauses in transaction documents, to provide for ownership to revert to the government in the event of a default or abandonment by the contractor.[20]

Fourth Circuit Says No Standing If Not an "Interested Party"

In last year's *Year in Review*, the authors reported on the unsuccessful efforts of the Baltimore Gas and Electric Company (BG&E) and the Maryland Public Service Commission (PSC) to challenge an Army solicitation to privatize the utility distribution system at Fort Meade, Maryland, in federal district court.[21] While BG&E elected not to appeal the district court's decision, the PSC sought relief from the Fourth Circuit Court of Appeals (Fourth Circuit), which dismissed the appeal for lack of jurisdiction after determining that the PSC was not an "inter-

13. Memorandum, Deputy Secretary of Defense, to Secretaries of the Military Departments, subject: Department of Defense Reform Initiative Directive 49—Privatizing Utility Systems (23 Dec. 1998).

14. Memorandum, Deputy Secretary of Defense, to Secretaries of the Military Departments, subject: Revised Guidance for the Utilities Privatization Program (9 Oct. 2002) [hereinafter Revised Guidance Memo]. According to this memorandum, the DOD changed its goal as a partial result of comments from the utility industry that the volume of "more than 1300 utility systems . . . either in the solicitation phase or pending release of a request for proposal . . . would saturate the market, resulting in decreased competition." *Id.*

15. *Id.* at 1. The new "milestone" will be considered "satisfied when the Source Selection Authority makes a decision or the Defense Component submits an exemption." *Id*.

16. *Id*.

17. *Id*. at 3-4, app. B (reproducing a copy of Memorandum, General Counsel of the Department of Defense, to General Counsels of the Military Departments, subject: The Role of State Laws and Regulations in Utility Privatization (24 Feb. 2000)).

18. *Id*. at 10. Federal Acquisition Regulation section 31.205-20 generally classifies interest on borrowings as an unallowable cost. GENERAL SERVS. ADMIN. ET AL., FEDERAL ACQUISITION REG. 31.205-20 (July 2002).

19. Revised Guidance Memo, *supra* note 14, app. E (reproducing a copy of Memorandum, Director, Defense Procurement, to Directors of Defense Agencies, subject: Class Deviation—Interest Costs (15 Apr. 2002)). The class deviation further provides:

> [T]he utilities privatization contractor will be permitted to recover its interest costs associated only with capital expenditures to acquire, renovate, replace, upgrade, and/or expand utility systems, and the contractor will not be permitted to receive *facilities capital cost of money* as a contract cost under FAR 31.205-10, Cost of money.

Id.; *see also* Memorandum, Defense Contract Audit Agency, to Regional Directors, subject: Audit Guidance on CAS and FAR Part 31, Cost Principles Applicability to Utility Privatization Contracts (4 June 2002) (providing additional guidance about the Cost Accounting Standards and the FAR Part 31 costing principles, as applied to utility privatization contracts).

20. Revised Guidance Memo, *supra* note 14, at 12.

21. Major John J. Siemietkowski et al., *Contract and Fiscal Law Developments of 2001—The Year in Review*, ARMY LAW., Jan./Feb. 2002, at 119-20 (discussing Baltimore Gas & Elec. Co. v. United States, 133 F. Supp. 2d 721 (D. Md. 2001)). Before filing suit in the district court, BG&E was also party to a GAO bid protest in 2000, which challenged the same Army solicitation on similar grounds. The GAO denied the protest. Virginia Elec. & Power Co., Baltimore Gas & Elec., Comp. Gen. B-285209, B-285209.2, Aug. 2, 2000, 2000 CPD ¶ 34. For a more complete discussion of that decision, see Major Louis A. Chiarella et al., *Contract and Fiscal Law Developments of 2000—The Year in Review*, ARMY LAW., Jan. 2001, at 61 [hereinafter *2000 Year in Review*].

ested party" under the Administrative Dispute Resolution Act[22] (ADRA), and therefore lacked standing.[23]

At the U.S. District Court for the District of Maryland (District Court), BG&E and the PSC, as an intervenor, argued that the Army's request for proposals (RFP) to privatize the electrical and natural gas distribution systems at Fort Meade failed to include provisions requiring an offeror to hold franchise rights and a PSC license, or one specifying that the PSC would have jurisdiction over the successful offeror.[24] The District Court found that the Army reasonably interpreted the applicable federal laws when it decided not to include such provisions in the solicitation.[25] On appeal, the PSC challenged that part of the District Court's decision that held that the Army did not have to require the successful offeror to submit to PSC jurisdiction. Because BG&E was no longer a party to the action, the Fourth Circuit found itself confronted with the issue of whether the PSC even had standing to challenge the Army RFP under the ADRA.[26]

The Fourth Circuit began by noting that in passing the ADRA, Congress granted standing to an "interested party objecting to a solicitation by a federal agency," but it left the term "interested party" undefined.[27] Next, the court observed that the Court of Appeals for the Federal Circuit (CAFC) had only recently clarified the use of the term "interested party" in the context of bid protests in the Court of Federal Claims (COFC), the primary federal court venue for bid protests.[28]

To understand the CAFC's views, the Fourth Circuit examined *American Federation of Government Employees, AFL-CIO v. United States*,[29] in which the CAFC reviewed the ADRA's legislative history to determine what meaning to give the term "interested party" in the context of the ADRA. Ultimately, the CAFC held that when Congress used the term "interested party" in the ADRA, it was cognizant that it had used the same term in the Competition in Contracting Act (CICA),[30] another bid protest jurisdiction-granting statute. The court concluded, therefore, that Congress must have "intended the same standing requirements that apply to protests under the CICA to apply to actions brought under [section] 1491(b)(1)" of the ADRA.[31] Finding the CAFC's analysis "sufficiently persuasive," the Fourth Circuit adopted it and applied the CICA standard to the ADRA. The court reasoned that because PSC's interest in the solicitation was "based solely on its desire as a state regulatory body to assert jurisdiction over the private entity that would eventually provide utility services at Fort Meade," it was neither an actual or prospective bidder or offeror. The Fourth Circuit thus held that the PSC did not have standing to bring a bid protest action or to appeal the District Court's decision.[32] Major Huyser.

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22. 28 U.S.C. § 1491(b)(1) (2000).

23. Maryland Pub. Serv. Comm'n v. United States, 290 F.3d 734 (4th Cir. 2002).

24. *Id*. at 735.

25. *Id*. at 736 (citing *Baltimore Gas & Elec*., 133 F. Supp. 2d at 721 (D. Md. 2001).

26. *Id*. The District Court had similarly questioned whether the PSC had standing to bring suit. The District Court avoided this issue, however, because another party, BG&E, the local Maryland utility the PSC had licensed in the Fort Meade area, satisfied the standing requirements. *Id*. (citing *Baltimore Gas & Elec*., 133 F. Supp. 2d at 727 n.8).

27. *Maryland Pub. Serv. Comm'n*, 290 F.3d at 736-37.

28. *Id*. at 737. The Fourth Circuit stated that it was "especially interested" in the CAFC's views on the subject, given the CAFC's "exclusive appellate jurisdiction over all ADRA cases filed on or after January 1, 2001" resulting from Congress's inclusion of a "sunset provision" in the ADRA. *Id*. (citing Impresa Construzioni Geom. Domenico Garufi v. United States, 238 F.3d 1324, 1331-32 (Fed. Cir. 2001) (discussing the pre-1997 bid protest jurisdiction of the federal district courts and the COFC)). Because the *Public Service Commission* plaintiffs filed suit before this sunset date, the Fourth Circuit would have had jurisdiction over the appeal if it determined that the PSC had standing. *Id.*; *see also 2000 Year in Review*, *supra* note 21, at 36-38 (discussing the end of bid protest jurisdiction in the federal district courts).

29. 258 F.3d 1294 (Fed. Cir. 2001).

30. *See* 31 U.S.C. § 3551(2) (2000) (defining "interested party" as "an actual or prospective bidder or offeror whose direct economic interest would be affected by the award of the contract or by failure to award the contract").

31. *Maryland Pub. Serv. Comm'n*, 290 F.3d at 739 (quoting Am. Fed'n of Gov't Employees, AFL-CIO v. United States, 258 F.3d 1294, 1302 (Fed. Cir. 2001)).

32. *Id*.

Construction Contracting

If You Throw Enough Mud Against a Wall, Something Will Stick

In *Comtrol, Inc. v. United States*,[1] Comtrol appealed a decision from the U.S. Court of Federal Claims (COFC) that granted a government motion for summary judgment. Comtrol had sued for various expenses arising from a contract with the Federal Aviation Administration (FAA) for construction work at the Salt Lake City International Airport. Comtrol sought reimbursement for: (1) differing site conditions and defective specifications based on the presence of quicksand at the work site;[2] (2) differing site conditions and defective specifications based on the placement of a fuel pipeline; (3) additional costs relating to alleged improvements to three underground duct banks; (4) additional overhead, time, and acceleration costs resulting from numerous change orders; and (5) damages resulting from an alleged breach of the government's implied contractual duties of cooperation, non-interference with contract performance, and good faith and fair dealing. Applying basic black-letter law procurement law, the U.S. Court of Appeals for the Federal Circuit (CAFC) denied the first two portions of Comtrol's appeal and remanded the remaining issues to the COFC for further consideration.[3]

The appellant based its differing site condition (quicksand) claim on a soil report that the government included in the contract by reference.[4] This report stated that "hard material . . . may be encountered," but generally characterized the soil at the site as consisting of a "relatively soft gray clay," and noted that the surveyors encountered ground water at the depth of two feet at several test sites.[5] Comtrol argued that the government misled it into believing that the soil at the site was dryer than it was; Comptrol argued that it was entitled to recovery under a Type I differing site condition theory.[6]

The CAFC dismissed this portion of the claim because Comtrol never reviewed the report before submitting its bid. Although the government incorporated the soil report into the contract by reference, Comtrol failed to obtain and review the document before submitting its bid. Because a contractor needs to establish reasonable reliance to prevail in a Type I differing site condition claim, the CAFC deemed Comtrol's arguments concerning the report's substance to be irrelevant and dismissed this portion of the appeal.[7]

Concerning the second claimed expense, increased costs associated with working around a fuel line that was not listed in the specifications, the CAFC observed that a pipeline drawing the agency provided to Comtrol noted that there was a pipeline on the excavation site. According to the CAFC, a reasonably alert contractor would have sought clarification from the government about the matter. As such, the CAFC concluded that Comtrol could not establish a differing site condition or defective specification claim because it was not reasonably prudent in interpreting the contract documents.[8]

The third portion of Comtrol's claim involved additional costs associated with changes to several duct banks that the FAA had ordered because of the wet soil conditions Comtrol encountered. At trial, the COFC granted summary judgment to the government for this portion of the claim, under the theory that the contractor bore the risk of additional costs associated with the wet site conditions, and as such, was required to pay for this work because it was a remedial to the extent that it was necessary to complete contract performance. Because of the paucity of facts in the record on this part of the claim, the CAFC could not determine whether the work was in fact remedial, or in the alternative, unrelated to the soil conditions. The CAFC remanded that portion of the claim for further consideration.[9]

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1. 294 F.3d 1357 (Fed. Cir. 2002).

2. The Differing Site Conditions (DSC) clause at FAR section 52.236-2 allows for an equitable adjustment if the contractor provides prompt, written notice of a differing site condition. To recover for a Type I Differing Site Condition, the contractor must prove that: (1) the contract either implicitly or explicitly indicated a particular site condition; (2) the contractor reasonably interpreted and relied on the contract indications; (3) the contractor encountered latent or subsurface conditions that differed materially from those indicated in the contract; and (4) the claimed costs were attributable solely to the differing site condition. GENERAL SERVS. ADMIN. ET AL., FEDERAL ACQUISITION REG. 52.236-2 (July 2002) [hereinafter FAR]; *see also* P.J. Dick, Inc., GSBCA No. 12036, 94-3 BCA ¶ 27,073; Franklin Pavkov Constr. Co., HUD BCA No. 93-C-C13, 94-3 BCA ¶ 27,078; Glagola Constr. Co., ASBCA No. 45579, 93-3 BCA ¶ 26,179; Konoike Constr. Co., ASBCA No. 36342, 91-1 BCA ¶ 23,440; Meredith Constr. Co., ASBCA No. 40839, 93-1 BCA ¶ 25,399.

3. *Comtrol*, 294 F.3d at 1359.

4. *Id*. at 1362-63.

5. *Id*. at 1360.

6. *Id*. at 1359-60.

7. *Id*. at 1362-63.

8. *Id*. at 1365.

9. *Id*. at 1366.

The fourth issue involved a request for equitable adjustment involving 142 change orders that Comtrol insisted were unrelated to the differing site conditions encountered at the work site. The CACF concluded that at least a few of the change orders were unrelated to the differing site conditions, and as such, remanded this issue to the COFC for further proceedings.[10]

Finally, Comtrol argued that the FAA violated its implied contractual duty to cooperate and not interfere with Comtrol's contract performance. Once again, the CAFC had no alternative but to remand this issue to the COFC because resolving the differing site condition issue did not automatically resolve this portion of the appeal.[11]

Not So Fast: CAFC Holds General Disclaimer Does Not Shift the Risk of a Design Flaw to the Contractor

In *Edsall Construction Co.*,[12] the Armed Services Board of Contract Appeals (ASBCA) determined that the government could not shift the responsibility for defective design specifications to a contractor with a general disclaimer. The CAFC recently examined the case and reached the same conclusion.[13]

The Army awarded Edsall a fixed-price construction contract for a facility to house Montana National Guard helicopters. The facility specifications included two hangars with 21,000-pound tilt-up canopy doors. The government included detailed design specification for a complex system of motors, cables, and pulleys, and counterweights to open and close the doors.[14] A general disclaimer provision in the contract stated that bidders were responsible for verifying the design before bidding, and "any condition that will require changes from the plans must be communicated to the architect for his approval prior to bidding and all of those changes must be included in the bid price."[15]

During the construction of the facility, Edsall encountered numerous problems with the door design. The design was unworkable; Edsall had to deviate from the government-provided design, at considerable expense to Edsall. Edsall submitted a claim to the contracting officer in the amount of $70,000 for costs attributed to the government's faulty design. The contracting officer rejected the claim because Edsall did not request the design change before bidding, as the disclaimer allegedly required. Edsall appealed this decision to the ASBCA.[16]

The ASBCA found that the specifications for the door incorporated a defective design. The board further found that Edsall's pre-bid review of the specifications was reasonable, and that the disclaimer on one drawing did not shift the risk of design inadequacies to Edsall.[17] On appeal, the government fared no better. The CAFC reasoned that "[w]hen the Government provides a contractor with a design specification, such that the contractor is bound by contract to build according to the specifications, the contract carries an implied warranty that the specifications are free from design defects."[18] With that said, "[g]eneral disclaimers requiring the contractor to check plans and determine project requirements do not overcome the implied warranty, and thus do not shift the risk of design flaws to contractors who follow the specifications."[19]

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10. *Id.* at 1366-67.

11. *Id.* at 1367. Comtrol argued that the COFC erred by dismissing, *sua sponte*, its breach of contract claim, which sought damages from the FAA for "breach of its implied contractual duties of cooperation, non-interference with work, and good faith and fair dealing." *Id.* The CAFC's decision does not explain in detail how the FAA allegedly breached this duty. *Id.*

12. ASBCA No. 51787, 01-2 BCA ¶ 31,425.

13. White v. Edsall Constr. Co., Inc., 296 F.3d 1081 (Fed. Cir. 2002); *see also* Major John J. Siemietkowski et al., *Contract and Fiscal Law Developments of 2001—The Year in Review*, ARMY LAW., Jan./Feb. 2002, at 87 [hereinafter *2001 Year in Review*].

14. *Edsall*, 296 F.3d at 1083. For a detailed description of the door design, see *2001 Year in Review*, *supra* note 12, at 87.

15. *Edsall*, 296 F.3d at 1083.

16. *Id.*

17. *Edsall*, 01-2 BCA ¶ 31,425, at 155,181; *see also 2001 Year in Review*, *supra* note 12, at 88.

18. *Edsall*, 296 F.3d at 1084.

19. *Id.* at 1085.

Examining the ASBCA's logic, the CAFC noted that the board, by sustaining Edsall's appeal, did not render the language of the disclaimer meaningless. The CAFC reasoned that the language "canopy door details . . . must be verified by the contractor"[20] could reasonably mean that the contractor should check the physical details of the door's weight and dimensions without altering the design itself. The language of the disclaimer did not negate the government's implied warranty that the specifications were free from defects.[21]

Interestingly, this decision does not necessarily preclude the government from shifting the risk in design specification contracts. The court clearly noted that the Army could have drafted specifications that shifted the risk of design defects to the contractor, but that the disclaimer on the drawing was simply not specific enough to shift the risk in this case.[22] If the government had incorporated an express disclaimer, as opposed to the general disclaimer used in this case, the results may have been different.

Eternal Vigilance Is the Price of Contracting with the Government

A recent CAFC decision reinforces the lesson that contractors doing business with the government must exercise at least a minimal degree of due diligence. In *Franklin Pavkov Construction* (*FPC*),[23] the Air Force awarded the appellant a firm fixed-price contract to install four sets of three-story stairs on two dormitory style buildings at Shaw Air Force Base, South Carolina. Under the contract, the Air Force provided government furnished property (GFP) for use in the construction of the stairs. The appellant was to construct the stairs in accordance with Air Force drawings and specifications, the same drawings and specifications it used in the solicitation for bids.[24] Although the Air Force awarded the contract in 1995, it had (unsuccessfully) attempted to implement a similar project in the same buildings in 1991. The Air Force down-scoped the project from the 1991 version after encountering problems with it.[25]

Before the award, the solicitation for bids was to contain a set of 1995 specifications as well as the 1995 drawings. A government employee, however, inadvertently gave FPC a copy of the 1991 specifications from the prior unsuccessful project. The Air Force did not firmly establish the existence of the mistake until a government inspector compared his copy of the 1995 specifications with FPC's 1991 version. Unfortunately, the project was ninety percent completed by this point.[26]

FPC also alleged that the Air Force provided FPC with defective GFP for the project.[27] Although the contract was silent about the means and date of delivery of the GFP, the parties agreed to delivery in November 1995, at a location about 100 to 200 yards from the job site. The Air Force delivered the GFP on the agreed date; however, FPC failed to inventory it until several months latter. On 14 May 1996, about five months after delivery, FPC informed the government that the shipment of GFP did not contain several "stair nosings," devices used to prevent slipping on the stairs. Because manufacturing the stair nosings required a considerable amount of lead time, the government agreed to use a substitute aluminum channel.[28]

When it completed the project, FPC submitted a certified claim to the contracting officer for $117,129, for costs allegedly associated with the defective specifications, defective and missing GFP, and a differing site condition involving a drain grate for which the government directed additional work.[29] The contracting officer denied FPC's claim; FPC appealed to the ASBCA.[30] The ASBCA held that the appellant was entitled to increased costs associated with the drain grate, but denied FPC's claims relating to defective specifications and defective GFP.[31]

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20. *Id.* at 1086.

21. *Id.*

22. *Id.*

23. 279 F.3d 989 (Fed. Cir. 2002).

24. *Id.* at 991.

25. *Id.* at 991-92.

26. *Id.* at 992.

27. *Id.* at 996.

28. *Id.* at 992.

29. *Id.* at 993.

30. *See* Franklin Pankov Constr. Co., ASBCA No. 50828, 00-2 BCA ¶ 31,100.

31. *Id.* at 153,609.

The ASBCA reasoned that the allegedly defective specifications did not give FPC a basis for recovery because the 1995 specifications had down-scoped the project from the 1991 specifications. The board reasoned that even if it would have been easier for FPC to perform the work according to the 1995 specifications, FPC still performed the project it bid on—the stairways—using the 1991 specifications.[32]

The ASBCA held FPC's feet to the proverbial fire concerning the defective GFP. The board noted that paragraph (c) of the government-furnished property clause provided that upon delivery of the GFP, the contractor assumed the risk and responsibility for the loss.[33] In this case, over five months elapsed from the date of delivery until FPC notified the government that the equipment was missing. In the absence of timely notice that the GFP was deficient, the board held that the appellant could not recover for the missing equipment.[34]

On appeal, the CAFC twice adopted the reasoning of the ASBCA. The court noted that the mix-up with the specifications created "no additional costs flowing proximately from the defect" because the defective specifications did not require FPC to do any work above the project it bid on.[35] Concerning the deficient GFP, the CAFC observed that FPC failed in its duty to inspect and inventory the GFP. Because the government could have cured any deficiencies in the GFP if it had timely notice, the court determined that FPC should not be allowed to collect from the Air Force for this portion of its claim.[36]

Government Can't Trump a Mandatory FAR Provision

Withholding progress payments may make good business sense when a contractor is verging on default, but excessive withholding will not win many points with the ASBCA. In *All-State Construction* (*All-State*),[37] the Navy awarded All-State a contract to construct a hazardous waste storage facility. Section 01010 of the contract provided as follows:

> The obligation of the government to make any payments under any of the provisions of this contract shall in the discretion of the Officer in Charge of the Construction, be subject to . . . [a]ny claims which the government may have against the Contractor under or in connection with this contract.[38]

The general provisions of the contract, however, included FAR section 52.232-5, "Payments Under Fixed-Price Construction Contract (April 1989)," which limits "retainage" of progress payments for unsatisfactory performance to ten percent of the amount of the payment "until satisfactory progress is achieved."[39]

As contract performance progressed, All-State encountered various delays, the excusability of which the parties disputed. On several occasions, the government accepted revised completion schedules from All-State. On each occasion, the government expressly stated that it was accepting the revised schedules to mitigate damages and did not waive its right to assess liquidated damages or terminate the contract for default. As work progressed, All-State invoiced the government for progress payments seven times. The government accepted and paid the first six invoices, subject to some retainage. The government rejected the seventh invoice, however, after the contracting officer determined that "it is not prudent at this time to make further payments to you until we are sure that sufficient funds are available in the contract to cover costs of reprocurement and the assessment of liquidated damages if the contract is terminated for default."[40]

Before the government received the seventh invoice, it paid All-State $211,573.50; it had retained $33,100 for liquidated delay damages and other expenses. When the government received Invoice Number 7, it had retained a total of $127,198.67, thirty-eight percent of All-State's undisputed earned amount for the work it had completed.[41] This amount was more than three times the maximum allowed by the FAR Payments Clause at FAR section 52-232-5.[42] Shortly after the

32. *Id.* at 153,608.

33. *Id.*

34. *Id.* at 153,609.

35. Franklin Pankov Constr. Co., 279 F.3d 989, 996 (Fed. Cir. 2002).

36. *Id.* at 998; *see supra* Part III.D (discussing *Pankov* and other GFP issues).

37. ASBCA No. 50586, 02-1 BCA ¶ 31,794.

38. *Id.* at 157,020.

39. *Id.* at 157,019; *see also* FAR, *supra* note 2, at 52.232-5(e).

40. *All-State*, 02-1 BCA ¶ 31,794, at 157,020.

41. *Id.*

government rejected Invoice Number 7, All-State stopped work on the contract. The contracting officer then terminated the contract for default, and All-State appealed the default termination to the ASBCA.[43]

Upon receipt of All-State's motion for summary judgment, the board examined the legal effect of section 01010 of the contract, and whether the government breached the contract by retaining more than three times maximum allowed under the FAR. The board found that section 01010 of the contract contradicted the clear wording of the FAR Payments Clause. Since the FAR Payments Clause is mandated by regulation, the board concluded that the government could not benefit by inserting a contradictory clause. As such, the contradictory clause was without legal effect.[44] The board then determined that retaining thirty-eight percent of progress payments otherwise due to All-State constituted a government breach of the contract. Finally, the board determined that the government's refusal to provide progress payments, as required under the Payments Clause, justified All-State's work stoppage.[45]

Eichleay, *Schmeichleay*

The *Construction* section of the *Year in Review* would not be complete without at least passing mention of two *Eichleay*[46] delay cases. In *Williams v. White*,[47] the government awarded Williams, the appellant, a firm fixed-price contract to make various improvements and repairs on a building at a medical center in Colorado. As with many construction contracts, Williams encountered several delays, and upon completion of the project, invoiced the government for $98,642 for "extended overhead/unabsorbed overhead."[48] The agency denied the claim, and Williams appealed the claim to the ASBCA. After an evidentiary hearing, the board issued an opinion denying Williams's delay claim. In its opinion, the board stated that it adopted the conclusion of a Defense Contract Audit Agency auditor that the delay costs had been fully absorbed into the base contract price.[49]

Williams appealed the ASBCA's decision to the CAFC. On appeal, the CAFC expressed considerable concern that the ASBCA had simply adopted the auditor's opinion without making an independent determination. The court expected the board to have made its own findings to that effect, rather than "merely stating that the auditor had so found."[50] The CAFC was also disturbed that the board failed to examine two prerequisites for establishing recovery under the *Eichleay* formula: (1) that the contractor was on standby; and (2) that the contractor was unable to take on other work.[51] As a parting shot, the CAFC noted that it was not disagreeing with the board, but rather could not make a determination based on this record. The CAFC remanded the case to the board.[52]

A second COFC case stands for the proposition that the court will not sustain a delay claim that does not neatly fit the *Eichleay* formula. In *Nicon, Inc. v. United States*,[53] the COFC examined whether a contractor could recover for alleged unab-

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42. *Id.* at 157,020; *see also* FAR, *supra* note 2, at 52.232-7.

43. *All-State*, 02-1 BCA ¶ 31,794, at 157,020. Several days after the government terminated All-State's performance, All-State proposed a settlement with the government for this and other disputes, which would have increased the contract price by $330,191.27. *Id.*

44. *Id.* at 157,021.

45. *Id.* at 157,020.

46. *See* Eichleay Corp., ASBCA 5183, 60-2 BCA ¶ 2,688, *recons. denied*, 61-1 BCA ¶ 2,894; *see also* West v. All State Boiler, Inc., 146 F.3d 1368, 1377 (Fed. Cir. 1998) ("[R]ecovery under the *Eichleay* formula is an extraordinary remedy designed to compensate a contractor for unabsorbed overhead costs that accrue when contract completion requires more time than originally anticipated because of a government-caused delay."). Under the *Eichleay* formula, unabsorbed overhead is calculated by multiplying the total cost incurred during the contract period by the ratio of billings for the delayed contract to total billings of the firm during the contract period. The daily contract overhead rate equals the allocable contract overhead divided by the days of contract performance. The recoverable amount equals the daily contract overhead rate multiplied by the number of days of government-caused delay. *See, e.g.*, Capital Elec. Co. v. United States, 729 F.2d 743 (Fed. Cir. 1984).

47. Charles G. Williams Constr., Inc. v. White, 271 F.3d 1055 (Fed. Cir. 2001).

48. *Id.* at 1057. Specifically, Williams calculated its unabsorbed overhead at $468 per day, which it multiplied by 330 (the total number of days of government-caused delay), for a total of $98,642. *Id.*

49. *Williams*, 271 F.3d at 1058 (citing Charles G. Williams Constr., Inc., ASBCA No. 49775, 00-2 BCA ¶ 31,047, at 153,321).

50. *Id.* at 1059.

51. *Id.* at 1058. The logic of this portion of the opinion is questionable. Had the board made a clear and unequivocal determination that the contract absorbed the overhead costs instead of simply restating the opinion of the auditor to that effect, there would be no reason to continue with this portion of the *Eichleay* analysis. The question of whether the contractor was on standby or otherwise unable to take on additional work is irrelevant if the base contract costs absorbed the overhead costs.

52. *Id.* at 1060.

53. 51 Fed. Cl. 324 (2001).

sorbed overhead costs resulting from a government delay in issuing a notice to proceed, in a contract that the government terminated for convenience before the beginning of performance.[54] Concluding that the *Eichleay* formula is the exclusive means available for calculating unabsorbed overhead resulting from a government-caused delay, the COFC ruled that a contractor cannot recover under *Eichleay*, or any other formula, if it has not begun to perform under a contract.[55] Major Dorn.

54. *Id*. at 324.

55. *Id*. at 328; *see also supra* Part IV.G (discussing the cost allowability aspects of the *Williams* and *Nicon* decisions).

Bonds, Surety, and Insurance

The Government Is Not a Nanny

In Westchester Fire Insurance Co.,[1] the Court of Federal Claims (COFC) recently stated that the government is "not a nanny" for sureties that are less than diligent in protecting their interests vis-à-vis the government and its contractors.[2] The COFC required the surety to pay the government's reprocurement costs, even though the surety alleged that the government abused its discretion in its administration of the contract.[3]

In Westchester, the Coast Guard contracted with Zanis Contracting Corporation (Zanis) for a waterfront rehabilitation project at the Coast Guard facility at Eaton's Neck, New York.[4] Shortly after the award, Zanis furnished a performance bond for the project that listed Westchester Fire Insurance Company (Westchester) as the surety.[5] The contract incorporated the Davis-Bacon Act (DBA), which provides that workers on the job must be paid no less than the prevailing rates for the area.[6] The contract also authorized the contracting officer to withhold payments from the contractor if the contractor failed to pay its workers the Department of Labor (DOL) specified rates.[7]

Zanis' performance was less than stellar; the contracting officer issued several cure notices for various unexcused delays. The contracting officer provided Westchester copies of these notices as he issued them. The contracting officer also learned that a subcontractor was not paying several of its employees in accordance with DBA pay rates.[8] Despite the delays, Zanis made some progress on the project, and on 7 June 1994, the contracting officer approved a $32,940 progress payment.[9] On 15 June 1994, however, the Coast Guard issued Zanis a default termination notice for, among other deficiencies, "repeated lack of performance" and "repeated failure to ensure proper wage deficiencies are corrected."[10]

Shortly after termination, the DOL initiated an investigation of the DBA violations. On 21 November 1994, the DOL requested that the contracting officer withhold $69,105.12 in back wages due to the employees. The contracting officer complied with the DOL's request.[11] Several months later, the DOL reached a settlement with the subcontractor, allowing the Coast Guard to release $60,216.58 of the withheld funds to the General Accounting Office (GAO) for disbursement to the effected employees. The contracting officer applied the remaining $8888.54 towards reprocurement costs.[12]

Before the DOL reached a settlement with the subcontractor, the contracting officer entered into discussions with Westchester about a possible surety takeover of the contract.[13] During negotiations, Westchester expressed an interest in entering into a surety takeover agreement, but as a condition to the agreement, Westchester insisted that the agency make the funds withheld because of the DBA violations available for the follow-on contract. The contracting officer refused, and after completing the requirement, awarded the follow-on contract to another contractor.[14]

Upon completion of the project, the contracting officer issued a final decision assessing reprocurement costs against Westchester. Westchester appealed the contracting officer's decision to the COFC and filed a complaint seeking reversal of the contracting officer's decision. Specifically, Westchester alleged that the Coast Guard's demand for payment was erroneous as a matter of law because Westchester was entitled to the

1. Westchester Fire Ins. Co. v. United States, 52 Fed. Cl. 567 (2002).

2. *Id*. at 579.

3. *Id*. at 587.

4. *Id*. at 569.

5. *Id*. at 570.

6. 40 U.S.C. § 276a (2000).

7. *Westchester*, 52 Fed. Cl. at 569-70.

8. *Id*. at 571.

9. *Id.* The Coast Guard reduced this amount from the $42,821 that Zanis had requested, because of the its concern over the rate of performance, and questions about "previous payroll reports." *Id.*

10. *Id*. at 571-72.

11. *Id*. at 572.

12. *Id*. at 573-74.

13. *Id*. at 573.

14. *Id*. at 574.

money the Coast Guard set aside as a result of the DBA violation. Westchester also asserted that it was entitled to the amount of the progress payment that the Coast Guard paid Zanis because the Coast Guard owed Westchester a contractual duty to act with "reasoned discretion" in its administration of the contract.[15] The government filed a counterclaim, asserting that Westchester was liable to the Coast Guard, based on its performance bond for $151,449.58, which represented the excess costs the government had to pay under the reprocurement contract (minus the $8888.54 reduction of identified DBA violations).[16]

The COFC examined both issues Westchester raised and concluded that Westchester's arguments were without merit. First, concerning the progress payment, the court observed that, by definition, a surety agreement is designed to protect the government's interests, and not the surety's.[17] Thus, the government only owes the surety a duty once the surety informs the government that a contractor may be in default; as such, the surety could become a party to the bonded contract. Absent notice from the surety, the "Government's equitable duty to act with reasoned discretion"[18] towards the surety was never triggered. Further, it was not the government's responsibility "to divine the surety's thinking process, or act as a nanny for the surety and ask whether . . . it would like the Government to withhold progress payments to the contractor."[19]

Second, the court held that the government's withholding of money pursuant to the DBA violation was not a "voluntary act" on the part of the government, as alleged by Westchester.[20] Rather, the money represented unpaid earnings of the subcontractor's workers who had priority over the contractor's assignee to the funds. In the words of the court, "[A] surety cannot acquire by subrogation rights that the contractor itself did not have."[21]

Don't Call Us, They'll Call You

The Court of Appeals for the Federal Circuit (CAFC) will generally hear an appeal from a board of contract appeals only if the board's decision resolves all issues presented to the contracting officer in the contractor's claim.[22]

In United Pacific Insurance Co. v. Roche,[23] the CAFC recently ruled that a board decision that failed to list which claims were subject to a surety takeover agreement did not resolve all of the presented issues; the CAFC therefore declined jurisdiction.[24] In United Pacific, the appellant issued a performance bond on behalf of Castle Abatement Corporation (Castle) for a contract involving the repair of a secondary containment system at McGuire Air Force Base, New Jersey.[25] Castle discontinued work on the project once it began incurring substantial expenses for environmental remediation as a result of unanticipated soil contamination at the site. As the surety, United Pacific then entered into a takeover agreement with the government and arranged for completion of the project. Several months later, United Pacific filed a request for equitable adjustment, consisting of ten claims totaling $1,759,966.80. The basis for the claims was the differing site conditions Castle and the surety allegedly encountered.[26] The contracting officer granted a small portion of the claim, but denied most of the expenses United Pacific sought.[27] United Pacific then appealed

15. *Id.* Specifically, Westchester alleged that the government violated its duty to act with reasoned discretion towards Westchester when the contracting officer paid Zanis the $32,940 progress payment immediately before issuing the notice of default termination. *Id*. at 574-75.

16. *Id*. at 572-75.

17. *Id.*

18. *Id*. at 576.

19. *Id*. at 579.

20. *Id*. at 581.

21. *Id.* As icing on the cake, the COFC awarded the Coast Guard interest on the judgment. Although Westchester argued that it was not subject to the FAR clause requiring the payment of interest "from the date due" because it never entered into a takeover contract with the government, the court rejected Westchester's reasoning. The COFC noted that as a surety for the contracting parties, Westchester was liable for all amounts the contractor owed to the government, including interest. *Id.* at 584-87; *see also* GENERAL SERVS. ADMIN. ET AL., FEDERAL ACQUISITION REG. 52.232 (July 2002) [hereinafter FAR].

22. *See* AAA Eng'g & Drafting, Inc. v. Widnall, 129 F.3d 602 (Fed. Cir. 1997).

23. United Pac. Ins. Co. v. Roche, 294 F.3d 1367 (Fed. Cir. 2002).

24. *Id.* at 1370.

25. *Id.* at 1368-69.

26. *Id*. at 1369.

27. *Id*. at 1368-69.

the decision to the Armed Services Board of Contract Appeals (ASBCA).[28]

The government filed a motion to dismiss the portions of the appellant's claims that arose before the takeover agreement for lack of jurisdiction.[29] In a slip opinion, the ASBCA granted the government's motion, but retained jurisdiction over the post-takeover portions of the equitable adjustment claims. The ASBCA opinion did not define which claims arose before the takeover agreement.[30] United Pacific appealed the decision to the CAFC. The government argued the ASBCA's decision was not final pursuant to the Contract Disputes Act.[31] The CAFC agreed with the government and dismissed the case. Specifically, the court noted that the decision was not final because it did not reach the full extent of the contracting officer's decision, which included a determination of the allowable quantum of the appellant's claims.[32]

No Cutting Corners on the Road to Paradise

In *Paradise Construction Co.*,[33] the GAO denied a bid protest when the Air Force found the protestor's bid bond defective, because it limited the surety's obligation to the difference between the protestor's bid amount and the amount of any replacement contract. In *Paradise*, the protestor bid on an Air Force contract for sealing four maintenance hangar roofs.[34] The invitation for bids (IFB) incorporated Federal Acquisition Regulation (FAR) section 52.228-1,[35] which provides that a bidder's failure to furnish the required bid guarantee in the proper format and amount "may be cause for rejection of the bid."[36] Further, subsection 1(e) provided that "[i]n the event the contract is terminated for default, the bidder is liable for any costs of acquiring work that exceeds the amount of its bid, and the bid guarantee is available to offset the difference."[37] The Air Force concluded, and GAO later agreed, that this meant that a defaulting bidder would be liable for any reprocurement costs that the government may incur, and if the bidder failed to pay those costs, the bond would be available for that purpose.[38]

In response to the IFB, Paradise submitted a bid bond that provided that the surety would "pay to the obligee [the government] the difference not to exceed the penalty thereof between the amount specified in said bid and such larger amount for which the obligee may in good faith contract with . . . to perform the work covered by said bid."[39] The Air Force found that the quoted language rendered the bond nonresponsive because it limited the surety's obligation to the difference between the amount bid by Paradise and the amount of any new contract in the event Paradise defaulted. As such, it failed to cover additional expenses that the government could incur.[40] The GAO agreed, finding the bid-bond as submitted was a "significant diminution of the defaulting bidder's and its surety's obligation under FAR [section] 25.228-1 to pay all reprocurement costs (up to the penal amount)." As such, the protestor's bid was nonresponsive to the RFP.[41]

Bonds? We Don't Need No Stinking Bonds!

Under FAR section 28.103-1,[42] agencies should generally not require performance bonds for contracts that do not involve

28. United Pac. Ins. Co., ASBCA No. 52419, 01-1 BCA ¶ 31,296.

29. *United Pac.*, 294 F.3d at 1369. The motion argued that as a surety, United Pacific did not independently possess standing to pursue the claims of Castle, and that without an assignment by Castle to United Pacific, only Castle was in contractual privity with the government for such claims. *Id.*

30. *Id.* at 1369.

31. *Id.* at 1370; *see also* 41 U.S.C. §§ 606, 607(d) (2000).

32. *United Pac.*, 294 F.3d at 1370.

33. Paradise Constr. Co., Comp. Gen. B-289144, Nov. 26, 2001, 2001 CPD ¶ 192.

34. *Id.* at 1.

35. FAR, *supra* note 21, at 52.228-1.

36. *Id.* at 52.228-1(e).

37. *Paradise Constr.*, 2001 CPD ¶ 192, at 1.

38. *Id.* at 1-2.

39. *Id.*

40. *Id.*

41. *Id.* at 2-3.

42. FAR, *supra* note 21, at 28.103-1.

construction. Although the FAR allows for a number of limited exceptions,[43] in *Apex Support Services, Inc.*,[44] the GAO concluded that the General Services Administration (GSA) failed to establish how its contract fit into any of those exceptions. In *Apex*, the contractor protested a GSA RFP for a service contract involving the inspection and acceptance of construction work for the government. The solicitation included requirements for a bid guarantee and a performance bond.[45] Before issuing the RFP, the contracting officer documented the reasons for requiring a bond for this contract in a memorandum. The memorandum stated that bonding was necessary to protect the government's interests because, among other reasons, the contractor would have the use of government property, the government did not have the means to perform the services in the event the contractor defaulted, and "the health, welfare, and morale of visitors and employees . . . would be negatively affected should the contractor fail to perform."[46]

The GAO examined each of these stated reasons and concluded they were all valid reasons for requiring a performance bond. The facts of this case, however, simply did not fit any of these stated reasons. Specifically, the GSA failed to demonstrate to the GAO's satisfaction how a disruption in services would jeopardize anyone's health, safety, or welfare, or why the GSA would have difficulty in reprocuring the services should the contractor fail to perform. There was nothing so unique about this contract that the GSA should deviate from the general rule. As such, the government acted unreasonably in requiring a performance bond in this case.[47] Major Dorn.

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43. *Id.* at 28.103-2. This provision allows for the use of bonds for service contracts when it is necessary to protect the government's interests. The FAR gives four examples of such situations, which include:

> where the government will provide the contractor property or funds for its use or as partial compensation; where the government wants assurance that a contractor's successor-in-interest is financially capable; where the government must make substantial progress payments before delivery begins; and where the contract is for dismantling, demolition, or removal of improvements.

Id. The GAO has opined that this list is not exhaustive and that there may be other circumstances where a bond is necessary to protect the government's interest. *See also* RCI Mgmt., Inc., Comp. Gen. B-228225, Dec. 30, 1987, 87-2 CPD ¶ 642.

44. Comp. Gen. B-288936, B-288936.2, Dec. 12, 2001, 2001 CPD ¶ 202.

45. *Id.* Specifically, the RFP required a bid guarantee in an amount equal to twenty percent of the bid amount for the base period of performance, and a performance bond in an amount equal to twenty percent of the contract price for the initial twelve-month period. *Id.*

46. *Id.* at 3.

47. *Id.* at 3-4.

Cost and Cost-Accounting Standards

Allowable Relocation Costs Ceiling Raised

This past year, the Federal Acquisition Regulation[1] (FAR) Council issued a final rule relating to the allowability of certain employee relocation costs.[2] The FAR Council had initially proposed to eliminate the $1000 ceiling on the allowability of miscellaneous relocation costs if the employee uses the lump-sum basis. The FAR Council ultimately concluded, however, that "[t]o reduce the Government's risk in this area, the final rule maintains a ceiling for miscellaneous expenses when a contractor uses the lump-sum payment method, but increases the limit from $1000 to $5000."[3] If the employee's reimbursement was based upon actual allowable expenses, however, there is no ceiling for this cost principle except reasonableness.[4] The final rule also added two new categories of allowable relocation costs: (1) payments for increased employee income or Federal Insurance Contributions Act (FICA) taxes incident to reimbursed relocation costs; and (2) payments for spouse employee assistance.[5]

In response to comments that the proposed rule may increase claimed costs for reimbursable relocation costs, the FAR Council noted that the cost principles should ensure that contractors are treated fairly, and that the cost principles should not be used as a cost containment mechanism.[6]

Payments for Extended Leave Benefits to Activated Reservists Are Allowable

In a memorandum dated 5 October 2001,[7] the Under Secretary of Defense for Acquisition, Technology, and Logistics, E.C. Aldridge, Jr., announced that a government contractor's continuation of certain fringe benefits for Guard and Reserve members activated in response to the September 11 terrorist attacks would be considered an allowable cost under FAR section 31.205-6, "Compensation for Personal Services."[8] Under Secretary Aldridge referred to these fringe benefits as extended military leave benefits, which also included any payment for the difference between the activated employee's civilian and military salaries. He also noted that many companies have chosen to provide these extended military leave benefits voluntarily for past similar mobilizations and applauded these companies' efforts to help mitigate the hardships for activated Guard and Reserve members.

Subsequently, the Defense Contract Audit Agency (DCAA) published audit guidance that amended the DCAA Contract Audit Manual's (DCAAM) coverage for the extended military leave benefits. Paragraph 7-2117.2 of the DCAAM originally provided guidance on the allowability of extended military leave benefits to contractor employees who served during Operations Desert Shield and Desert Storm.[9] Interestingly, the amended paragraph does not specifically limit the allowability for extended military leave benefits to those Guard and Reserve members activated in response to the 11 September terrorist attacks and would presumably be an allowable cost for any subsequent call to active military duty.[10]

"How Would You Like Your Books Cooked—Rare, Medium or Well Done?" Refund of Previously Reimbursed State Taxes Through a Cost-Reimbursement Contract Is Allocated Back to the Government

The Court of Appeals for the Federal Circuit (CAFC) recently affirmed a Court of Federal Claims (COFC) decision allowing the government to recover its $4,725,000 allocable portion of a $10.5 million tax refund it received in 1995 for a 1987 Virginia tax that had been reimbursed as an allowable and allocable contract cost under a prior cost-reimbursement contract.[11] The prior cost-reimbursement contract was for the operation of an ammunition plant in Virginia. The disputed tax

1. General Servs. Admin. et al., Federal Acquisition Reg. (July 2002) [hereinafter FAR].

2. Federal Acquisition Circular 2001-08, 67 Fed. Reg. 43,512 (June 27, 2002). The council also amended the relocation cost allowability rules. FAR, *supra* note 1, at 31.205-35.

3. 67 Fed. Reg. at 43,516.

4. *Id.*

5. *See* FAR, *supra* note 1, at 31.205-35(a)(10)-(11).

6. 67 Fed. Reg. at 43,519.

7. Memorandum, E.C. Aldridge, Jr., Under Secretary of Defense, Acquisition, Technology, and Logistics, to Directors of Defense Agencies, Deputy for Acquisition and Business Management, ASN(RD&A), Deputy Assistant Secretary of the Air Force (Contracting), SAF/AQC, Deputy Assistant Secretary of the Army (Procurement), ASA(ALT), Executive Director, Logistics Policy & Acquisition Management (DLA), subject: Allowability of Contractor Costs for Employees Who Perform Active Military Duty in Conjunction With the Current National Emergency (5 Oct. 2001) [hereinafter Aldridge SRP Memo].

8. *See* FAR, *supra* note 1, at 31.205-6.

9. *See* U.S. Dep't of Defense, Defense Contract Audit Agency, DCAAM 7640.1, DCAA Contract Audit Manual para. 7-2117.2 (Jan. 2001) [hereinafter DCAAM].

refund resulted from the sale of a joint venture interest by Hercules Incorporated that Virginia taxed as a capital gain. Hercules sought reimbursement of its 1987 Virginia income and franchise tax liability, including the capital gain tax, on a direct cost allocation method between its Virginia operations. After an initial government denial of the requested reimbursement attributable to the capital gains tax, Hercules and the government stipulated to a reimbursable cost of $4,870,466 in the initial COFC proceeding.[12]

Subsequently, in 1995, Hercules received a $10.5 million Virginia tax refund attributable to the 1987 capital gains tax on the joint venture sale. In the subsequent COFC hearing and CAFC appeal, Hercules argued that the Cost Accounting Standards (CAS)[13] provided for tax refunds to be recorded as a reduction to the tax costs of the year in which the refund was received. Presumably, Hercules preferred this method of accounting in 1995 because it had started operating the plant on a firm fixed-price contract basis on 1 January of that year. If the cost-reimbursement contract had still been in place, the tax refund would have reduced Hercules' tax costs; the government's reimbursement would also have been lower because of the tax refund.

The government, of course, wanted its allocable portion of the tax refund using the same methodology used to allocate and reimburse the 1987 tax costs under the prior cost-reimbursement contract. Specifically, the government argued that FAR sections 31.205-41(d), 52.216-7(h)(2), and 31.201-5 "clearly instruct that any refund of a tax that has been allowed as a contract cost must be credited or paid to the government utilizing the same factors by which the costs were originally determined to be reimbursable."[14]

On appeal of the COFC's grant of summary judgment in the government's favor, the CAFC agreed with the government's interpretation. The CAFC also determined that the applicable FAR clauses did not conflict with the CAS because the CAS does not specifically address "how to calculate the amount of contractor liability to the government for tax refunds that have been allocated and reimbursed pursuant to the contracts that were in force during the tax year."[15] Accordingly, the CAFC seemed to draw a distinction between the applicability of the CAS for contract cost accounting and reporting and FAR clauses that directly relate to the financial matters between contracting parties.

"Did I Say That?"
CAFC Essentially Rejects Its Prior Holding in the Northrop Decision

Recently, in *Boeing North America, Inc. v. Roche*,[16] the CAFC explained and justified its analysis in *Caldera v. Northrop Worldwide Aircraft Services, Inc.* (*Northrop*)[17] to the maximum extent possible without actually overruling it altogether. In its 1999 *Northrop* decision, the CAFC ruled that legal costs were unallowable where the agency incurred the costs as the result of an unsuccessful defense of a wrongful termination suit. Four former employees who claimed they were discharged for refusing to participate in fraud against the Army brought the wrongful termination suit. The court reversed an earlier Armed Services Board of Contract Appeals (ASBCA) case and applied a "government benefit" analysis for allowability using the allocation principles of FAR section 31.201-4. In reversing the ASBCA, the court reasoned as follows:

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10. The amended version of the DCAAM states:

> a. Many companies choose to continue certain fringe benefits, such as health insurance, for employees who have been called to military duty. In addition, many companies pay these individuals the difference between their civilian and military salaries in an effort to help mitigate the hardships that those called to active military duty will experience. In accordance with an October 5, 2001 memorandum issued by the Under Secretary of Defense for Acquisition, Technology and Logistics, these types of supplemental benefits for extended military leave are to be considered allowable costs pursuant to FAR 31.205-6, Compensation for personal services.
> b. Allowable amounts are limited to the lesser of (a) the contractor's extended military leave benefits plus active duty pay, or (b) the total compensation of an employee at the time of entry into active military duty. For purposes of computing this limitation, active duty pay includes basic pay, all specialty pay, and all allowances, except for subsistence, travel, and uniform allowances.

Id. para. 7-2117.2.

11. Hercules, Inc. v. United States, 292 F.3d 1378 (Fed. Cir. 2002) [hereinafter *Hercules III*], *aff'g* Hercules, Inc. v. United States, 49 Fed. Cl. 80 (2001) [hereinafter *Hercules II*].

12. *See* Hercules, Inc. v. United States, 22 Cl. Ct. 301 (1991) [hereinafter *Hercules I*].

13. *See Hercules II*, 49 Fed. Cl. at 86; *Hercules III*, 292 F.3d at 1381. *Hercules III* specifically cited CAS 406, 48 C.F.R. § 9904.406-20, and CAS 410, *id.* § 9904.410-20. *Hercules III*, 292 F.3d at 1381.

14. *Hercules III*, 292 F.3d at 1381.

15. *Id*.

16. 283 F.3d 1320 (Fed. Cir. 2002).

17. 192 F.3d 962 (Fed. Cir. 1999).

> It is established that the contractor must show a benefit to government work from an expenditure of a cost that it claims is "necessary to the overall operation of the [contractor's] business." The Board erred in failing to make a determination of whether or not [the contractor's] defense of the Oklahoma lawsuit benefited the government. We can discern no benefit to the government in a contractor's defense of a wrongful termination lawsuit in which the contractor is found to have retaliated against the employees for the employees' refusal to defraud the government.[18]

This confusing analysis, which improperly mixed principles of allocability and allowability, subsequently reared its ugly head in *Boeing*. Boeing appealed a contracting officer's final decision that denied reimbursement for attorneys' fees and expenses related to a shareholders' derivative suit against the directors of Boeing's predecessor, Rockwell International Corp. (Rockwell).[19] The derivative suit alleged that Rockwell's directors failed to enforce adequate internal controls and fostered a climate that led to employee misconduct, resulting in criminal and civil corporate liability. The parties eventually settled the derivative suit with Rockwell, agreeing to pay the shareholders' legal fees and expenses and to indemnify the defendant directors against their attorneys' fees and expenses.[20]

Boeing claimed that FAR section 31.205-33 allowed the attorneys' fees and expenses as professional and consultant service costs. The government contended that the disputed costs were not allocable under FAR section 31.201-4 because there was not a beneficial relationship between the disputed costs and the contract requirements. The board held for the government, reasoning as follows:

> The rationale of *Northrop* can properly extend to the facts of this appeal so as to bar the allocability of the disputed costs under FAR 31.201-4(c). We can discern no benefit to the Government in a contractor's defense of a third party lawsuit in which the contractor's prior violations of federal laws and regulations were an integral element of the third party allegations.[21]

When properly interpreted, however, the benefit analysis for determining allocability under FAR section 31.201-4 is not related to a specific identifiable government benefit, but relates to an accounting concept as the CAFC described on appeal as follows:

> Allocability is an accounting concept involving the relationship between incurred costs and the activities or cost objectives (e.g., contracts) to which those costs are charged. Proper allocation of costs by a contractor is important because it may be necessary for the contractor to allocate costs among several government contracts or between government and non-government activities.[22]

The question of whether a cost is an allowable cost under a government contract is a separate analysis conducted only after the contract activity determines whether the cost is allocable. In *Boeing*, the court distinguished the concepts of allowability and allocability, reasoning, "The concept of cost allowability concerns whether a particular cost can be recovered from the government in whole or part. Allowability of a cost is governed by the FAR regulations, i.e., the cost principles expressed in Part 31 of the FAR and pertinent agency supplements."[23]

Accordingly, the CAFC held that the word "benefit" in FAR section 31.201-4(b) describes a nexus for accounting purposes and is not meant to allow an inquiry into whether the cost sufficiently benefits the government or not.[24] Although the CAFC agreed with Boeing on the proper concept of allocability, it did not agree that the costs were allowable as professional and consultant service costs.[25] Using the similarity test under FAR section 31.204(c)—because FAR section 31.205 did not directly address the allowability of this specific cost—the CAFC applied the cost allowability principles under FAR section 31.205-47, for similar legal proceedings brought by the government or through a relator under the False Claims Act.[26] Specifically, the third party relator settlement scenario of FAR section 31.205-47(c)(2),[27] which allowed reasonable costs if a contract-

18. *Id.* at 972 (citations omitted).

19. Boeing North America, Inc., ASBCA No. 49994, 00-2 BCA ¶ 30,970.

20. *Id.* at 152,844.

21. *Id.* at 152,848.

22. *Boeing*, 283 F.3d at 1326.

23. *Id.*

24. *Id.* at 1328.

25. *See* FAR, *supra* note 1, at 31.205-33.

ing officer determined that there was very little likelihood that a third party would prevail on the merits, was most similar.

The CAFC also conceded that its *Northrop* decision "has caused confusion about why the costs in question were not allowable."[28] The CAFC, however, backed up its *Northrop* decision as follows: "Properly understood, Northrop and FAR § 31.205-47 establish a simple principle—that the costs of unsuccessfully defending a private suit charging contractor wrongdoing are not allowable if the 'similar' costs would be disallowed under the regulations."[29]

The CAFC ultimately concluded that the board committed legal error by misapplying the allocability benefit analysis for allowability purposes. The CAFC then remanded the case to the board with the direction that the "[b]oard may allow the costs only if it determines that the plaintiffs in the [derivative] lawsuit had 'very little likelihood of success on the merits' of prevailing."[30]

"Oh, We're Not Through Yet"—The CAFC Vacates and Revises Its Earlier Boeing Decision

On 29 July 2002, the CAFC vacated its 15 March 2002 *Boeing* decision[31] and issued a revised opinion.[32] The CAFC's substantive conclusion that vacated and remanded the case to the ASBCA, however, remained unchanged. Essentially, the CAFC revised its discussion and references concerning the concept of allocability. Originally, the court had discussed the accounting concept of allocability in reference to FAR section 31.201-4.[33] In the revised opinion, the court held that "[c]ost allocability here is to be determined under the Cost Accounting Standards ('CAS'), 4 C.F.R. Parts 403, 410."[34] The court also noted the "general proposition that 'costs may be assignable and allocable under CAS, but not allowable under [the FAR].'"[35] The court then engaged in a complex discussion of the degree to which their earlier decision in *Northrop* bound them.[36] Specifically, the court questioned "whether we are also bound by the court's conclusion that the costs were not allocable because they did not benefit the government."[37] The court ultimately concluded, "Under our established precedent we are not bound by *Northrop* on the issue of allocability under the CAS standards since the CAS issue was neither argued nor discussed in our opinion."[38]

The CAFC once again remanded the case to the ASBCA, with the same direction as its vacated decision that the "[b]oard may allow the costs only if it determines that the plaintiffs in the [derivative] lawsuit had 'very little likelihood of success on the merits' of prevailing."[39]

The ASBCA Considers Appeal on the Allowability of Legal Defense Costs

Not content watching the CAFC jump through hoops to clarify *Northrop* in the two *Boeing* appeals, the ASBCA waded into the deep morass of legal defense cost allowability yet again. In *General Dynamics Corp.*,[40] the ASBCA held that a contractor may recover legal costs for a successful defense against government False Claims Act allegations, even if the contractor failed to successfully defend against other fraud allegations in the same lawsuit. To apportion the allowable successful defense

26. 31 U.S.C. § 3729 (2000).

27. *See* FAR, *supra* note 1, at 31.205-47(c)(2).

28. *Boeing*, 283 F.3d at 1327.

29. *Id.* at 1331.

30. *Id.* at 1334.

31. *Id.*

32. Boeing North America, Inc. v. Roche, 298 F.3d 1274 (Fed. Cir. 2002).

33. *Boeing*, 283 F.3d at 1326.

34. *Boeing*, 298 F.3d at 1280. The court clarified that the CAS provisions were subsequently codified at 48 C.F.R. pts. 9903-04. *Id.* at 1280 n.6.

35. *Id.* (citing United States v. Boeing Co., 802 F.2d 1390, 1394 (Fed. Cir. 1986)).

36. Caldera v. Northrop Worldwide Aircraft Svcs., Inc., 192 F.3d 962, 962 (fed. Cir. 1999).

37. *Boeing*, 298 F.3d at 1281.

38. *Id.* at 1283 (citations omitted).

39. *Id.* at 1290.

40. ASBCA No. 49372, 02-2 BCA ¶ 31,888.

costs from unallowable unsuccessful defense costs[41] under FAR section 31.205-47,[42] however, the ASBCA held that: (1) the successfully defended claims must not stem from the same wrongdoing as the unsuccessfully defended claims; and (2) there must be a reasonable basis to apportion the costs.[43] Major Kuhn.

41. The unsuccessful defense costs related to a settlement between General Dynamics and the Government for claims of subcontractor bribes to General Dynamics. *Id.* at 157,551.

42. The FAR disallows the following legal expenses:

> (b) Costs incurred in connection with any proceeding brought by a Federal, State, local, or foreign government for violation of, or a failure to comply with, law or regulation by the contractor (including its agents or employees) . . . are unallowable if the result is—
>
> (1) In a criminal proceeding, a conviction;
>
> (2) In a civil or administrative proceeding, . . . a finding of contractor liability where the proceeding involves an allegation of fraud or similar misconduct . . . ;
>
> . . . .
>
> (4) Disposition of the matter by consent or compromise if the proceeding could have led to any of the outcomes listed in paragraphs (b)(1) through (3) of this subsection . . . .

FAR, *supra* note 1, at 31.205-47.

43. *See Gen. Dynamics Corp.*, 02-2 BCA ¶ 31,888, at 157,567.

Deployment and Contingency Contracting

Brown & Root Services Awarded LOGCAP Contract

In December 2001, the U.S. Army awarded the Logistics Civil Augmentation Program (LOGCAP) contract to Halliburton KBR Government Operations division (Halliburton KBR), formerly Brown & Root Services, a division of Halliburton KBR of Arlington, Virginia.[1] The LOGCAP is defined as "a U.S. Army initiative for peacetime planning for the use of civilian contractors in wartime and other contingencies."[2] Through the LOGCAP, the Army is laying the foundation for awarding an umbrella support contract—a firm-fixed-price contract for peacetime contingency planning. The Army would obtain logistics, engineering, and construction services necessary for specific contingency operations by issuing cost-plus-award-fee or cost-plus-fixed-fee delivery orders.[3]

The third award of the LOGCAP contract "is a [ten]-year Task Order contract, with a one-year base period and nine one-year options."[4] Brown & Root Services, the predecessor of Halliburton KBR, was the original LOGCAP contractor from 1992 to 1997. The Army subsequently awarded Brown & Root Services a two-year sole-source contract to continue its services, specifically in the Balkans. Beginning in 1999, the Army competitively awarded Brown & Root Services a five-year contract for logistics services in the Balkans.[5]

Update of Special Authorities Invoked in the Wake of the 11 September 2001 Attacks

As last year's *Year in Review* reported, the federal government invoked a number of special authorities in response to the 11 September terrorist attacks.[6] President Bush declared a national emergency on 14 September 2001 through his issuance of Proclamation 7463.[7] On the same day, he issued Executive Order (EO) 13,223, which authorized the service secretaries to order any unit or member of the Ready Reserve of the Armed Forces to Active Duty for not more than twenty-four months, and to order stop loss for active and reserve forces.[8]

Through EO 13,235,[9] President Bush invoked the emergency construction authority at 10 U.S.C. § 2808.[10] The President delegated the emergency construction authority to the Secretary of Defense, who further delegated the authority to the Secretaries of the military departments.[11] The President's prior declaration of a national emergency and the subsequent invocation of emergency construction authority allow the undertaking of "military construction projects, not otherwise authorized by law[,] that are necessary to support . . . the armed forces."[12]

President Bush continued his declaration of a national emergency for another year by issuing a notice on 12 September 2002,[13] continuing these emergency authorities and others that require the declaration of a national emergency.

Last year's *Year in Review* also noted[14] that the anti-terrorist operations in Afghanistan and elsewhere—Operation Enduring Freedom—were declared a contingency operation under 10 U.S.C. § 101(a)(13)(B).[15] This change increased the simplified

1. Press Release, Halliburton Corp., Halliburton KBR Wins Logistics Civil Augmentation Contract from US Army (Dec. 17, 2001) [hereinafter Halliburton Press Release], *available at* http://www.halliburton.com/news/archive/2001/kbrnws.

2. U.S. Dep't of Army, Army Materiel Command, AMC Pam. 700-30, Logistics Civil Augmentation Program 3 (LOGCAP) (31 Jan. 2000).

3. *Id.* at 5.

4. *See* Halliburton Press Release, *supra* note 1.

5. *Id.*

6. *See* Major John J. Siemietkowski et al., *Contract and Fiscal Law Developments of 2001—The Year in Review*, Army Law., Jan./Feb. 2002, at 98-99 [hereinafter *2001 Year in Review*].

7. Proclamation No. 7463, 66 Fed. Reg. 48,199 (Sept. 14, 2001).

8. Exec. Order No. 13,223, 66 Fed. Reg. 48,201 (Sept. 14, 2001).

9. Exec. Order No. 13,235, 66 Fed. Reg. 58,343 (Nov. 20, 2001).

10. 10 U.S.C. § 2808 (2000); *see also supra* Part V.D. (analyzing the construction funding aspects of this authority).

11. Exec. Order No. 13,235, 66 Fed. Reg. at 58,343.

12. 10 U.S.C. § 2808(a).

13. Continuation of the National Emergency with Respect to Certain Terrorist Attacks, 67 Fed. Reg. 58,317 (Sept. 12, 2002).

14. *See generally 2001 Year in Review*, *supra* note 6, at 98.

acquisition threshold at FAR section 101[16] from $100,000 to $200,000,[17] for acquisitions using the procedures of FAR part 13[18] to support contingency operations outside the United States.[19]

The amendment of DFARS section 213.301,[20] proposed before the 11 September attacks,[21] arrived just in time. This amendment allows contracting officers supporting contingency operations,[22] or humanitarian or peacekeeping operations,[23] to use the Government Purchase Card for purchases up to the increased $200,000 simplified acquisition threshold.[24] It remains to be seen, however, just how effective this authority will prove to be for operations in unsophisticated, cash-based economies such as Afghanistan.

Army Contracting Agency Is Deployable

On 22 August 2002, the Secretary of the Army, Thomas E. White, established the United States Army Contracting Agency (ACA).[25] The ACA, among other missions, is the Army's "primary point of contact for planning contingency contracting operations at the strategic and operational level to support the war-fighter worldwide."[26] To begin implementing this mission, the ACA established a Directorate of Contingency Contracting (DC^2) in its Falls Church, Virginia, headquarters. Under the ACA Implementation Plan,[27] the Director of DC^2 is the Army's Executive Agent for contingency contracting and operational contracting missions. The Director will coordinate and allocate ACA resources to support contingency and operational contracting requirements, update and develop Army and Joint doctrine affecting contingency contracting, and develop standard training guidance for contingency contracting personnel.[28] The Director also serves as the "FORSCOM/Army Service Component Command (ASCC) contingency contracting planner."[29] The ACA also plans to reorganize "contingency contracting such that the ACA operationally controls and evaluates [contingency contracting officers] CKOs [to] improve contracting support to the warfighter, and establish contingency contracting as a progressive career assignment."[30] Readers should expect

15. This provision states:

> The term "contingency operation" means a military operation that—
> (A) is designated by the Secretary of Defense as an operation in which members of the armed forces are or may become involved in military actions, operations, or hostilities against an enemy of the United States or against an opposing military force; or
> (B) results in the call or order to, or retention on, active duty of members of the uniformed services under section 688, 12301(a), 12302, 12304, 12305, or 12406 of this title, chapter 15 of [10 U.S.C. §§ 331-335], or any other provision of law during a war or during a national emergency declared by the President or Congress.

10 U.S.C. § 101(a)(13)(B).

16. GENERAL SERVS. ADMIN. ET AL., FEDERAL ACQUISITION REG. 2.101 (July 2002) [hereinafter FAR].

17. National Defense Authorization Act for Fiscal Year 2002, Pub. L. No. 107-107, § 836, 115 Stat. 1012, 1192 (2001). Section 836 of the National Defense Authorization Act for Fiscal Year 2002 increases the simplified acquisition threshold for DOD procurements of supplies or services that facilitate the defense against terrorism or biological or chemical attack to $250,000. The limit is $500,000 if the procurement is outside the United States. *Id*.; *see also supra* Part II.F.

18. *See* FAR, *supra* note 16, pt. 13.

19. *See, e.g.*, Memorandum, Acting Deputy Assistant Secretary of the Army (Procurement) to Commanders, Program Executive Officers, and PARCs, subject: Simplified Acquisition Threshold Increase in Support of Operation Enduring Freedom (10 Oct. 2001).

20. U.S. DEP'T OF DEFENSE, DEFENSE FEDERAL ACQUISITION REG. SUPP. 213.301 (July 1, 2002) [hereinafter DFARS].

21. 65 Fed. Reg. 56,858 (proposed Sept. 20, 2000).

22. *See* 10 U.S.C. § 101(a)(13) (2000).

23. *See id*. § 2302(8).

24. Defense Federal Acquisition Regulation Supplement, Overseas Use of the Purchase Card in Contingency, Humanitarian, or Peacekeeping Operations, 66 Fed. Reg. 55,123 (Nov. 1, 2001) (to be codified at 48 C.F.R. pt. 213).

25. Headquarters, Dep't of Army, Gen. Orders No. 6 (22 Aug. 2002) [hereinafter GO6].

26. *Id.* at 3.

27. U.S. DEP'T OF ARMY, IMPLEMENTATION PLAN, CONSOLIDATION OF U.S. ARMY CONTRACTING (29 Mar. 2002) [hereinafter ACA Implementation Plan] (on file with author).

28. *Id.* para. 6.4.1.

29. *Id.* para. 6.4.1.6.

interesting developments in the Army contingency contracting community.

Who Are You Going to Call for Air Force Contingency Contracting Support?

In a memorandum dated 1 October 2001, the Air Force Deputy Assistant Secretary for Contracting, Brigadier General Darryl A. Scott, clarified who is the Head of Contracting Activity (HCA) authority for Air Force contingency contracting officers (CCOs).[31] General Scott's purpose was "to clarify the language of AFFARS 5301.601-91(c), 5301.601-93(a) and Appendix CC, Part 2, Section CC-201."[32] In his memorandum, General Scott stated:

> For Contingency contracting officers (CCOs) deployed in support of JCS-declared contingency operations or exercises, the commander of the Air Force component command, tasked to support the "supported commander" (as defined in JP 1-02), is the HCA for contracting actions executed by the CCO, regardless of the geographic area of the CCO's deployment.[33]

General Scott recognized, however, that there are exceptions for CCOs who augment established contracting offices and for those contracting officers who provide collateral support.[34] Of course, prior planning and coordination by the unified command responsible for the operation with all supporting elements should go a long way toward establishing the "technical chain of command" supporting contracting officers. Major Kuhn.

30. *Id.* para. 6.1.

31. Memorandum, Deputy Assistant Secretary (Contracting) to the Air Force Assistant Secretary (Acquisition), to ALMAJCOM/FOA/DRU (CONTRACTING), subject: Head of Contracting Activity (HCA) Authority for Contingency Contracting (1 Oct. 2001) (on file with author).

32. *Id.* (citing U.S. DEP'T OF AIR FORCE, AIR FORCE FEDERAL ACQUISITION REG. SUPP. (8 May 2001)).

33. *Id.*

34. *Id.*

Environmental Contracting

Federal Agencies Continue to Struggle with "Recycled-Content" Purchases

Last year's *Year in Review*[1] highlighted a General Accounting Office (GAO) Report that discussed the difficulty federal agencies had in documenting their purchases of recycled-content items under the Resource Conservation and Recovery Act (RCRA) of 1976.[2] This past July, the Director of Natural Resource and Environmental Issues testified about RCRA compliance efforts before the Senate Committee on Environment and Public Works.[3] The Director's conclusions were similar to those in last year's report.

The Director's testimony focused on six federal agencies that submit annual purchase reports to the Office of Federal Procurement Policy and the Office of the Federal Environment Executive. He concluded that agencies report estimates instead of actual purchase data. Several of the agencies "[did] not clearly identify purchases of recycled-content products" and others "[did] not receive complete data from their headquarters and field offices or their contractors and grantees."[4] Only the Department of Defense's estimates could be characterized as "reliable."[5] Procurement agencies complain that the EPA's recycled-content list "contains more items than they can feasibly track" and that it is "costly and burdensome to update their tracking programs each time the EPA adds new items to the list."[6] Agencies also reported that they lack automated tracking systems for recycled-content products and experienced only limited success in efforts to promote awareness of the requirement to increase purchase recycled-content products.[7] This topic is likely to be the subject of discussion throughout the year.

Things Are Looking Greener Around Here

Two years ago, President Clinton signed an Executive Order (EO) entitled "Greening the Government Through Leadership in Environmental Management."[8] The Civilian Agency Acquisition Council (CAAC) and the Defense Acquisition Regulations Council (DARC) recently issued a proposed rule to amend the Federal Acquisition Regulation[9] to implement the EO.[10] The EO places responsibility on the head of each federal agency to integrate environmental accountability into short and long-term planning.[11] It also establishes environmental management goals through several initiatives, including "sound acquisition and procurement policies."[12] Specifically, the EO places limits on the purchases of toxic chemicals, hazardous substances, and other pollutants.[13] It also requires agencies to have acquisition and procurement practices that enhance "environmentally and economically beneficial practices."[14] Comments to the proposed rule were due no later than 28 October 2002.[15]

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1. *See* Major John J. Siemietkowski et al., *Contract and Fiscal Law Developments of 2001—The Year in Review*, ARMY LAW., Jan./Feb. 2002, at 104 (discussing GEN. ACCT. OFF., REP. NO. GAO-01-430, *Federal Procurement: Better Guidance and Monitoring Needed to Assess Purchases of Environmentally Friendly Products* (June 22, 2001)).

2. The Resource Conservation and Recovery Act of 1976, 42 U.S.C. §§ 6901-6992k (2000) [hereinafter RCRA], gives the Environmental Protection Agency (EPA) the authority to control hazardous waste from cradle to grave. It requires each procuring agency that purchases more than $10,000 of an item per fiscal year that the EPA has designated as available with recycled content to have an affirmative procurement program to ensure that the agency purchases recycled-content products to the maximum extent practicable. *See* 42 U.S.C. § 6962.

3. *See* GEN. ACCT. OFF., REP. NO. GAO-02-928T, *Federal Procurement: Government Agencies' Purchases of Recycled-Content Products* (July 11, 2002).

4. *Id*. at 5. The six federal agencies are the Departments of Defense, Energy, Transportation, Veterans Affairs; the General Services Administration; and the National Aeronautics and Space Administration. *Id.*

5. *Id*. at 6.

6. *Id*. at 7-8.

7. *Id*. at 9-13.

8. Exec. Order No. 13,148, 65 Fed. Reg. 24,595 (Apr. 26, 2000).

9. GENERAL SERVS. ADMIN. ET AL., FEDERAL ACQUISITION REG. (July 2002) [hereinafter FAR].

10. 67 Fed. Reg. 55,670 (proposed Aug. 29, 2002) (to be codified in scattered sections of 48 C.F.R. pts. 23, 52).

11. *See* § 101, 65 Fed. Reg. at 24, 595.

12. *Id*. § 204.

13. *Id*. § 701.

HAZMAT Safety Obligations Relief on the Way for Contractors?

On 4 January 2002, the CAAC and the DARC proposed another amendment[16] to the FAR that "seeks to align the safety standards for federal employees in connection with hazardous materials [HAZMAT] furnished under government contracts with the protections afforded nonfederal employees under the Occupational Safety and Health Act."[17] The OSHA and the Federal Hazard Communications Standard (FHCS) require chemical manufacturers and importers to label their products and to provide detailed workplace safety information on Material Safety Data Sheets (MSDS). The OSHA and the FHCS do not protect public sector employees. Instead, the FAR implements *FED-STD-313*, which provides virtually the same information on HAZMAT for government contracts.[18]

Presently, HAZMAT means "any material defined as hazardous under the latest version of Federal Standard No. 313 (including revisions adopted during the term of the contract)."[19] The proposed rule would delete the parenthetical phrase and limit the contractors' compliance obligations to the *FED-STD-313* version "in effect on the date of issuance of the solicitation."[20] The revision would allow a contracting officer to modify the contract if a revision to *FED-STD-313* occurs during the course of performance. The proposed rule also plans to delete the FAR section that expands contractors' liability beyond that of chemical suppliers to the private sector. The proposed rule adds a new FAR provision that clarifies the applicability of HAZMAT-related regulations.[21] It also includes a pledge from the DARC to address contractors' concerns about requiring excess information and releasing proprietary data and trade secrets.[22]

Indemnification Clause Requires More than Crying over Spilled Oil

In *Cross Petroleum v. United States*,[23] an oil provider had contracts for diesel and unleaded fuel deliveries to different tank locations in the Klamath National Forest (KNF). The contractor, Cross Petroleum Inc. (Cross), made the contract for diesel fuel directly with the U.S. Forest Service; the contract included a provision holding the contractor liable and responsible for costs associated with oil spills. Cross also supplied unleaded oil to the KNF through a separate arrangement with the Defense Logistics Agency (DLA).[24] The contracts with the DLA were identical to the local contract with the Forest Service. After an uneventful delivery of diesel fuel, the contractor deposited two thousand gallons of unleaded fuel into the wrong tank, which unfortunately was perforated. The Forest Service contracting officer issued a final decision against Cross "in the amount of $705,657.72 for costs associated with the spill."[25]

The Court of Federal Claims (COFC) denied the contractor's summary judgment motion, which alleged that the Forest Service contract for diesel fuel deliveries did not apply to the unleaded fuel deliveries. Instead the COFC found that "the facts concerning the nature of the parties' agreement are woefully underdeveloped."[26] The COFC also rejected the argument that the Forest Service contract did not encompass damage caused by unleaded fuel spills. Although the contract did not

14. *Id*. § 704. The GAO will generally defer to an agency's solicitation requirement that meets certain policy goals. In *Mark Dunning Industries, Inc*., Comp. Gen. B-289378, Feb. 27, 2002, 2002 CPD ¶ 46, the GAO rejected a prospective bidder's contention that requirements for an individual household weighing system and the use of a specific landfill site were unduly restrictive. The individual household weighing system was available to all contractors and would reasonably allow the government to meet the DOD's policy goals regarding trash disposal. *Id*. at 2. The use of the specific landfill site was reasonable because it offered the agency quick access in the event of unintended disposal of unexploded ordnance. *Id*. at 4.

15. *Mark Dunning Indus.*, 2002 CPD ¶ 46, at 4.

16. 67 Fed. Reg. 632 (proposed Jan. 4, 2002) (to be codified in scattered sections of 48 C.F.R. pts. 23, 52).

17. *Id*. The proposed amendment explained that "[t]he Occupational Safety and Health Act of 1970 (OSHA) and the Federal Hazard Communication Standard (FHCS) . . . provide protection for most of this nation's [private sector] employees against the hazards of exposure to domestically produced or imported chemicals." *Id*. (citing 29 C.F.R. § 1910.1200 (2002)).

18. FAR, *supra* note 9, subpt. 23.3.

19. *Id*. at 52.223-3(a).

20. *See* 67 Fed. Reg. at 634.

21. *Id.* at 633 (deleting FAR section 52.223-3(f), which states that "neither the requirements of this clause nor any act or failure to act by the Government shall relieve the contractor of any responsibility or liability for the safety of the Government, contractor, or subcontractor personnel or property").

22. *See Proposed FAR Rule to Ease Some Contract Obligations for HAZMAT Safety*, 44 GOV'T CONTRACTOR 1, ¶ 9 (Jan. 9, 2002) (discussing the proposed rule).

23. 51 Fed. Cl. 549 (2002).

24. *Id*. at 551-52.

25. *Id*. at 551.

explicitly mention "unleaded" fuel, "[t]he entire indemnity provision is cast in prophylactic terms" that required the contractor to "use reasonable care to avoid" damage and contamination, and addressed accidents involving "any" fuel.[27] The COFC found it "neither 'weird' nor 'inexplicable' that this provision should apply as long as [Cross] was in KNF in connection with the contract, and that the provision would continue to apply even though the parties made subsequent arrangements for additional deliveries in KNF."[28] Major Modeszto.

26. *Id*. at 553. The court noted that the contractor's own proposed findings of fact "reflect its own uncertainty as to whether the delivery of fuel to Oak Knoll was made under a 'blanket agreement' . . . , an informal 'open market' purchase, or the Forest Service's 'general authority for small purchases of miscellaneous supplies.'" *Id*.

27. *Id*. at 555.

28. *Id*. at 556.

Foreign Military Sales

"Dear Uncle Sam, Thank You So Much for Your Military Assistance. You Are Too Kind."

The General Accounting Office (GAO) recently reported that Saudi Arabia was the largest Middle Eastern recipient of military assistance,[1] receiving approximately $33.5 billion of military equipment under the Foreign Military Sales (FMS) program from fiscal year 1991 through fiscal year 2000.[2] With equipment transfers totaling almost $18 billion during the same ten-year period, Israel came in as the second-largest Middle Eastern recipient of military assistance.[3] The Middle East's largest recipient of U.S. military aid in the form of Foreign Military Financing grants was Israel, totaling over $19 billion. Egypt placed a close second, at $13 billion.[4]

Executive Order—National Emergency Housecleaning

In 1999, former President Clinton issued Executive Order (EO) 13,129,[5] which declared the Taliban's harboring of Osama Bin Laden and the al-Qaeda terrorist organization a national emergency.[6] After the U.S. military campaign successfully ousted the Taliban from power, President Bush issued Executive Order (EO)13,268, terminating EO 13,129.[7] Although the Taliban were no longer in control of Afghanistan, President Bush used EO 13,268 to add the Taliban and Mohammed Omar to the list of terrorist leaders and organizations identified in the national emergency declared in response to the terrorist attacks of 11 September 2001.[8]

President Bush also restored normal trade relations with Afghanistan through Proclamation 7553 of 3 May 2002.[9] Through Proclamation 7553, President Bush hoped to "facilitate increased trade [between the United States and Afghanistan], which could contribute to economic growth and assist Afghanistan in rebuilding its economy."[10] Subsequently, the State Department amended the International Traffic in Arms Regulations (ITAR) to allow the government to grant licenses or approve exports of defense articles or services to the current interim government of Afghanistan.[11]

President Bush Waives Missile Proliferation Sanctions Imposed on Pakistan and Continues Certain National Emergencies[12]

To support the war against terrorism, the State Department waived missile proliferation sanctions against Pakistan for those transactions needed to support Operation Enduring Freedom.[13]

In other actions, the President continued emergency declarations with respect to Weapons of Mass Destruction,[14] Iran,[15] Iraq,[16] Cuba,[17] and the former Yugoslavia.[18]

1. The GAO reported on five types of military assistance encompassing equipment, services, and training, including the Foreign Military Sales program, 22 U.S.C. §§ 2761-2770 (2000), the Foreign Military Financing program, 22 U.S.C. §§ 2763-2764, the International Military Education and Training program, 22 U.S.C. § 2347, the Excess Defense Articles authority, 22 U.S.C. § 2321j, and the Emergency Drawdown Authority, 22 U.S.C. § 2318. The Arms Export Control Act, 22 U.S.C. §§ 2751-2799, and the Foreign Assistance Act of 1961, 22 U.S.C. §§ 2151-2431 (as amended), govern all of these programs. *See* GEN. ACCT. OFF., REP. NO. GAO-01-1078, *Defense Trade: Information on U.S. Weapons Deliveries to the Middle East* (Sept. 20, 2001) [hereinafter GAO-01-1078].

2. GAO-01-1078, *supra* note 1, at 5.

3. *Id*.

4. *Id.* at 4 n.12.

5. Exec. Order No. 13,129, 64 Fed. Reg. 36,757 (July 7, 1999).

6. President Bush had last continued this national emergency declaration on 3 July 2001. 66 Fed. Reg. 35,363 (July 3, 2001).

7. Exec. Order No. 13,268, 67 Fed. Reg. 44,751 (July 3, 2002).

8. *Id.*

9. Proclamation No. 7553, 67 Fed. Reg. 30,535 (May 7, 2002).

10. *Id.* at 30,535.

11. Bureau of Political-Military Affairs: Amendment to the List of Proscribed Destinations in the International Traffic in Arms Regulations, 67 Fed. Reg. 44,352 (July 2, 2002) (to be codified at 22 C.F.R. § 126.1(g)).

12. The declaration of a national emergency makes available a number of extraordinary authorities under a variety of statutes. 50 U.S.C. § 1621 (2000). Emergencies are terminated either by presidential proclamation or by congressional actions. *Id.* § 1622.

13. Bureau of Nonproliferation; Waiver of Certain Missile Proliferation Sanctions Imposed on the Pakistani Ministry of Defense (MOD), 66 Fed. Reg. 56,892 (Nov. 13, 2001).

14. Continuation of Emergency Regarding Weapons of Mass Destruction, 66 Fed. Reg. 56,965 (Nov. 13, 2001).

"Sorry, No Act Today. Will an Executive Order Do?"

Last year, President Bush issued EO 13,222,[19] which declared a national emergency relating to the expiration of the Export Administration Act of 1979.[20] Through the issuance of EO 13,222, President Bush continued the provisions of the repealed Export Administration Act, the regulations established under the Act,[21] and delegations of authority, as if the Act was in full force and effect.[22] On 14 August 2002, President Bush signed Executive Order 13,222,[23] which continued the national emergency declaration for one year. The original declaration and the continuation were necessary because Congress failed to renew the Export Administration Act.[24]

State Department Export Licensing Procedures Need Improvement

The GAO recently criticized the State Department's export licensing procedures for processing delays, lost applications, and inconsistent licensing decisions.[25] The GAO reported that the lack of formal guidelines for determining when the State Department should refer license applications to other agencies was the primary cause of delays in the review process.[26] The GAO also stated that the State Department lacks adequate license tracking procedures, resulting in lost applications,[27] and that its licensing officers lacked adequate training, resulting in arbitrary and inconsistent results.[28] Subsequently, the State Department stated that it was planning and implementing a web-based export licensing program.[29] The GAO, however, characterized the State Department's proposed corrective action in its report as follows: "As we pointed out, past GAO work has proven that proceeding with information technology modernization without first correcting problems in current systems risks merely automating inefficient ways of doing business."[30]

Pick Your Poison—Commerce or State Jurisdiction Confusion for Missile Export Controls

The GAO also criticized the conflicting dual jurisdiction between the State Department and the Commerce Department over missile products and technology.[31] To "limit the proliferation of missiles capable of delivering nuclear, biological, and chemical weapons and their associated equipment and technology," the United States and six allies established the Missile Technology Control Regime (MTCR) in 1987.[32] The MTCR

15. Continuation of the National Emergency with Respect to Iran, 67 Fed. Reg. 11,553 (Mar. 14, 2002).

16. Continuation of the National Emergency with Respect to Iraq, 67 Fed. Reg. 50,339 (Aug. 1, 2002).

17. Continuation of the National Emergency Relating to Cuba and of the Emergency Authority Relating to the Regulation of the Anchorage and Movement of Vessels, 67 Fed. Reg. 9387 (Feb. 28, 2002).

18. Continuation of Emergency with Respect to the Federal Republic of Yugoslavia (Serbia and Montenegro), 67 Fed. Reg. 37,661 (May 29, 2002).

19. 66 Fed. Reg. 44,025 (Aug. 22, 2001).

20. *See* 50 U.S.C. §§ 2401-2419 (2000) (repealed 2001).

21. *See* 15 C.F.R. pts. 730-774 (2002).

22. Exec. Order No. 13,222, 66 Fed. Reg. 44,025 (Aug. 22, 2001).

23. 67 Fed. Reg. 53,721 (Aug. 16, 2002).

24. *See* Notice of August 14, 2002, 67 Fed. Reg. at 53,721 (Aug. 16, 2002); Exec. Order No. 13,222, 66 Fed. Reg. 44,025 (Aug. 22, 2001).

25. *See* GEN. ACCT. OFF., REP. NO. GAO-02-203, *Reengineering Business Processes can Improve Efficiency of State Department License Reviews* (Dec. 31, 2001) [hereinafter GAO-02-203].

26. *Id.* at 6.

27. *Id.* at 8.

28. *Id.* at 6-7.

29. *See State Department Plans Web-Based Export Licensing Program*, 44 GOV'T CONTRACTOR 2, ¶ 15 (Jan. 16, 2002).

30. GAO-02-203, *supra* note 25, at 15.

31. GEN. ACCT. OFF., REP. NO. GAO-02-120, *Export Controls: Clarification of Jurisdiction for Missile Technology Items Needed* (Oct. 9, 2001) [hereinafter GAO-02-120].

32. *Id.* at 3. The seven founding members of the MTCR are Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States. Since its founding in 1987, twenty-six other countries have joined the MTCR. *Id.* at 3 n.3.

established export policy guidelines and a list of controlled missile systems, components and technologies (hereinafter Regime items).[33]

The GAO reported, however, that the United States has established conflicting export control regulations to fulfill its MTCR responsibilities. Under the authority of the Arms Export Control Act,[34] the State Department uses the U.S. Munitions List established in the International Traffic in Arms Regulations[35] to control Regime items.[36] Alternatively, under the Export Administration Act of 1979,[37] the Commerce Department identifies dual-use items and technologies in the Commerce Control List of the Export Administration regulations[38] to control Regime items.[39] The GAO identified two factors that have contributed to unclear jurisdiction for missile sensitive items and technologies:

> First, officials at the Departments of Commerce and State have expressed different understandings of how to define which Regime items are Commerce Department-controlled and which are State Department-controlled.
>
> Second, consultations between the Departments of Commerce and State on Regime-related changes to their regulations have not ensured that items are clearly subject to the jurisdiction of one Department or the other.[40]

The GAO found that unclear jurisdiction may result in conflicting restrictions and reviews "which may affect U.S. national interests and companies' ability to export Regime items."[41] The GAO recommended a joint review of the Regime items between the Departments of Commerce and State to determine the appropriate jurisdictional control. It also recommended that the Commerce Department provide a cross-reference to the U.S. Munitions List if dual-use Regime items meet certain parameters that subject them to the State Department's jurisdiction.[42] Major Kuhn.

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33. *Id.* at 3.

34. 22 U.S.C. §§ 2751-2799 (2000).

35. 22 C.F.R. pts. 120-130 (2002).

36. GAO-02-120, *supra* note 31, at 4.

37. 50 U.S.C. §§ 2401-2419 (2000) (repealed 2001).

38. 15 C.F.R. pts. 730-774 (2002).

39. GAO-02-120, *supra* note 31, at 4.

40. *Id.* at 7.

41. *Id.* at 9.

42. *Id.* at 12.

Government Information Practices

Re-Solicitation of Service Contracts: New Limits on the Release of Unit Prices Under The Freedom of Information Act?

In *R & W Flammann GmbH v. United States*,[1] the United States Court of Federal Claims (COFC) decided a pre-award bid protest suit partially upon the government's disclosure of previous contract prices under the provisions of the Freedom of Information Act (FOIA).[2] The plaintiff, R & W Flammann GmbH (Flammann), was a German business entity that had contracted with the Army "to provide 'between occupancy maintenance' for the U.S. Government Housing facilities in Heidelberg, Germany."[3] Flammann, the "lowest-priced responsive bidder under a sealed bid solicitation," received the government award.[4] The contract, for one base year with four one-year options, was to run from 1 February 2001 through 31 January 2006; however, "[a]s early as October 2001, [the Army] expressed that it would *not* exercise the first-year option under the incumbent contract."[5] Instead, the Army intended to issue a new solicitation for a new contract.[6] During the second solicitation, and pursuant to a FOIA request, the government "released plaintiff's unit prices for the current and future [option] years to its competitor," SKE Gmbh (SKE).[7] The plaintiff filed suit on 18 July 2002, after the government dismissed the plaintiff's pre-award bid protest.[8]

The crux of the case was the nature of the government's second solicitation for the between-occupancy maintenance (BOM) services. The first contract followed sealed bid solicitations, but the "new" solicitation used "two-step bidding,"[9] in which the government issued an initial Request for Technical Proposals on 5 October 2001, and then issued an Invitation for Bids (IFB) on 2 July 2002.[10] While the court's opinion did not disclose the reason for the government's decision not to exercise the option,[11] it clearly stated that the government "characterizes" the second solicitation for BOM services "as a 'new' solicitation."[12] The government's position was "that the contracts are 'extremely different' due to . . . the change in the contract type from a requirement-type to an indefinite-type" and the additional requirement that each work crew include one English speaking person.[13] On the other hand, Flammann "observed by the Statement of Work that the re-solicitation is substantially similar to its incumbent contract."[14] In support of its view, Flammann reported that "some 87.5% of the [contract line item numbers (CLINs)] of the two contracts 'correspond directly.'"[15]

The court agreed that "[t]o the extent that the defendant is in fact soliciting for BOM services for the U.S. Government Housing facilities at Heidelberg, Germany, as was the case in the incumbent contract, the current solicitation *is* a re-solicitation."[16] The court, however, did not rest its opinion upon "the precise similarities (or differences, for that matter) between the

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1. 53 Fed. Cl. 647 (2002). Pursuant to a protective order from the Court of Federal Appeals, this case was filed under seal on 28 August 2002. Because neither party filed a notice or proposed redactions, the court's opinion was published on 23 September 2002. *Id*. at 648.

2. 5 U.S.C. § 552 (2000). The FOIA requires the government to release information upon request unless that information is exempt from release under one or more of the statute's exemptions. *Id*.

3. *Flammann*, 53 Fed. Cl. at 649. The "between occupancy maintenance," or BOM, "included carpentry, electrical, sanitation, interior painting, cleaning, stairwell maintenance, and floor repair, among other things." *Id.* at 648-49.

4. *Id*. at 649.

5. *Id.*

6. *Id*.

7. *Id*. at 648.

8. *Id*. at 650. The plaintiff's bid protest was based upon the government's release of plaintiff's contract unit prices. *Id.*

9. *See generally* GEN. SERVS. ADMIN. ET AL., FEDERAL ACQUISITION REG. 14.503 (July 2002) [hereinafter FAR] (outlining "two-step" sealed bidding procedures).

10. *Flammann*, 53 Fed. Cl. at 650.

11. The court did acknowledge in a footnote that it "is well settled that defendant may exercise its option at *its* discretion," and that "there is a (rebuttable) presumption of 'good faith' when government agents discharge their duties." *Id*. at 649 n.7 (citations omitted). The court was somewhat uncharitable in the text of the opinion, however. "To date, defendant has failed to provide plaintiff with a coherent explanation why it chose *not* to exercise its option." *Id.* at 649.

12. *Id*. at 649 n.4 (citing the government's reply brief).

13. *Id.* at 649 n.6 (citing the government's reply brief).

14. *Id*. at 649.

15. *Id*. at 649 n.6.

contracts, but rather on the germane issue of *fundamental fairness* in the procurement process."[17]

The court based its determination of fairness on the administrative record. According to the record, it was "undisputed" that the plaintiff's original contract bid became publicly available upon bid opening.[18] The record also reflects that the government decision not to exercise the option was not due to the plaintiff's performance; that the government invited the plaintiff to participate in the second solicitation; and that Flammann did submit a technical proposal and a subsequent bid. After issuing the Request for Technical Proposals, the government received SKE's FOIA request for a copy of Flammann's present contract.[19] On 20 November 2001, the government provided Flammann with "submitter notice"[20] of SKE's request.[21] While Flammann "warmly objected"[22] to the proposed disclosure, remarkably, it did not file a "reverse FOIA"[23] suit to enjoin the government's release. About five months[24] after providing notice to Flammann, the government released the plaintiff's contract to SKE.[25] Flammann then filed an agency protest, but an independent protest review official affirmed the contracting officer's decision. Flammann then sought injunctive relief from the COFC on 18 July 2002.[26] Shortly thereafter, a third successful step-one offeror, Facilma GmbH (Facilma), informed the government that it would not submit a step-two bid because the government's release of Flammann's contract price to just one bidder "violate[d] all applicable German and

16. *Id.* at 649 n.4.

17. *Id.* at 649 n.6. Aside from mentioning the positions taken by the parties in their written submissions and stating that the asserted "facts may be probative," the court did not discuss the merits of either side's arguments regarding the similarities or differences in the two contracts. *Id.* Later in the opinion, however, the court quickly dispatched the government's attempt to distinguish the two contracts:

> Defendant argues that the incumbent contract and the prospective contract are "extremely different." This is not so, and the court does not weigh the effects of the differences other than to observe and find that, on the face of the solicitation, the Statements of Work are, in fact, substantially similar in most, if not all, material particulars.

Id. at 655 (quoting the government's reply brief).

18. *Id.* at 653. The court correctly noted that,

> plaintiff's unit prices do not fit within Exemption 4 of FOIA, because publicly available information cannot meet part one of the *National Parks* "confidential" standard. . . . "[T]o the extent that any data requested under FOIA are in the public domain, the submitter is unable to make any claim to confidentiality—a *sine qua non* of Exemption 4."

Id. (quoting CNA Fin. Corp. v. Donovan, 830 F.2d 1132, 1154 (D.C. Cir. 1987)). Moreover, the court specifically acknowledged that "[b]idders are flatly precluded from protecting information submitted through sealed bids as proprietary information." *Id.* at 653 n.20 (citing Warner Labs., Inc., B-189502, 1977 U.S. Comp. Gen. LEXIS 1952 (Oct. 21, 1977). Interestingly, all of the bidders' contract prices became public upon the opening of the sealed bids. This result is in stark contrast to the protections afforded to the contract proposals of unsuccessful offerors submitted in response to solicitations for competitive proposals. Congress enacted this general restriction on the release of unsuccessful offeror's competitive proposals in 1996. *See* 10 U.S.C. § 2305(g) (2000).

19. *Id.* at 649. SKE GmbH requested the Flammann contract's "current cost schedule contained in the 'Supplies or Services and Price/Costs' section," which included "some 360 CLINs for the unit pricing of the current and future option years." *Id.* at 649 n.9.

20. *See* Exec. Order No. 12,600, 3 C.F.R. 235 (1987 Comp.), *reprinted in* 5 U.S.C. § 552 note (2000); *see also* U.S. DEP'T OF JUSTICE, OFFICE OF INFO. AND PRIVACY, VIII FOIA UPDATE 2, at 2-3 (1987). "Submitter notice" is the procedure whereby an agency provides pre-disclosure notice to a non-governmental source, when a third party has requested the information the non-governmental source provided to the agency. This administrative practice is governed by Executive Order 12,600, which requires each government agency "to establish pre-disclosure notification procedures which will assist agencies in developing adequate administrative records." U.S. DEP'T OF JUSTICE, OFFICE OF INFO. AND PRIVACY, JUSTICE DEPARTMENT GUIDE TO THE FREEDOM OF INFORMATION ACT 217 (2000) (citing 3 C.F.R. 235 (2000)) [hereinafter FOIA GUIDE]; *see generally* U.S. DEP'T OF DEFENSE, DIR. 5400.7-R, DOD FREEDOM OF INFORMATION ACT PROGRAM para. 5-207 (14 Apr. 1997) [hereinafter DODD 5400.7-R] (outlining Department of Defense "submitter notice" procedures).

21. *Flammann*, 53 Fed. Cl. at 649.

22. *Id.*

23. A "reverse FOIA" suit is an action in which the submitter of information, "'usually a corporation or other business entity' that has supplied an agency with 'data on its policies, operations or products—seeks to prevent the agency that collected the information from revealing it to a third party [usually] in response to the latter's FOIA request.'" FOIA GUIDE, *supra* note 20, at 640 (quoting CNA Fin. Corp. v. Donovan, 830 F.2d 1132, 1133 n.1 (D.C. Cir. 1987)).

24. According to its own guidelines, the government should have provided Flammann with a reasonable time to object to the release. *See* DODD 5400.7-R, *supra* note 20, para. 5-207a. Department of Defense components should give submitters thirty days to object to proposed disclosures, "unless it is clear that there can be no valid basis for objection." *Id.*

25. *Flammann*, 53 Fed. Cl. at 649.

26. *Id*.

European contracting rules as well as the ethics of fair competition."[27]

While "fundamental fairness" appears to be the basis of the court's decision, it is interesting to note that the plaintiff did not raise or pursue the issue of procurement integrity. The court found that the plaintiff "averred a vague inference that there may have been a modicum of bad faith on the part of the defendant in its failure to exercise option year one."[28] Even after the court's inquiry, however, the "plaintiff never developed any argument before the court to overcome the presumption of good faith on the part of the government."[29]

The court also interpreted the mere filing of Flammann's complaint as an implicit accusation of unfairness.[30] The gravamen of the plaintiff's complaint, however, was that its unit prices were exempt from public disclosure[31] under the Trade Secrets Act[32] and FOIA Exemption 4.[33] Flammann argued that under the *National Parks* test,[34] "it would suffer substantial competitive harm in the re-solicitation for a new contract covering largely the same time period and scope of work because it would be forced to 'ratchet down' its prices and/or otherwise could be underbid" by competitors.[35] Even after ruling that sealed bid contract prices were not exempt under the FOIA[36] and are generally not protected by the Trade Secrets Act,[37] the court returned to the issue of fairness, finding that the plaintiff's unit prices were only "*generally* subject to release under FOIA" and that "*under the peculiar facts at bar*," the government's release was arbitrary, capricious, or otherwise not in accordance with law.[38]

In the "peculiar facts at bar," an incumbent contractor was ostensibly providing a new contract bid for a contract period for which he arguably had a previous winning bid.[39] In this situation, there was more than a distinct possibility that Flammann's second bid would either be similar to its first contract or priced lower so as to remain viable against the "educated" bid of its competitor. In either situation, Flammann would be disadvantaged. For this reason, the court may have been persuaded that release of Flammann's incumbent contract prices was tantamount to the release of its second bid, prior to the bid opening.[40] Although the court did not explicitly cite this reasoning as a

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27. *Id.* at 650 n.10. Facilma GmbH's letter also averred that the government's actions "leave the impression that the sole purpose of the subject solicitation is the underbidding of the current contract unit prices." *Id.*

28. *Id*. at 649 n.7.

29. *Id*.

30. *Id*. at 655. "Plaintiff's contention [by this lawsuit] that it will be harmed clearly goes to an appearance or perception of impropriety." *Id.*

31. *Id*. at 651-52.

32. 18 U.S.C. § 1905 (2000).

33. 5 U.S.C. § 552b(4) (2000).

34. *See* Nat'l Parks and Conservation Assoc. v. Morton, 498 F.2d 765 (D.C. Cir. 1974). The *National Parks* decision outlined a test to determine whether information submitted to the government merited protection as "confidential" commercial or financial information under FOIA Exemption 4. The *National Parks* test, which is customarily viewed as consisting of two disjunctive prongs, provides Exemption 4 protection to information whose disclosure "would impair the government's future ability to obtain necessary information or cause substantial harm to the competitive position of the submitter." 5 U.S.C. § 552b(4); *see generally* FOIA GUIDE, *supra* note 20, at 187-221.

35. *Flammann*, 53 Fed. Cl. at 651. The "ratcheting-down" of prices by competitors is not the type of competitive harm typically contemplated by the *National Parks* test, however, the landmark decision of *McDonnell Douglas Corp. v. NASA*, 180 F.3d 303 (D.C. Cir 1999), recently applied this theory to the "ratcheting-down" of prices. *See* Major Timothy M. Tuckey, *The Changing Definition of Unit Prices: Another Blow to the Government's Efforts to keep the Public Informed?*, ARMY LAW., Dec. 2001, at 13 (analyzing *National Parks* and the government policy changes related to the release of contract unit prices).

36. *Flammann*, 53 Fed. Cl. at 653. In this case,

> [I]t is undisputed that sealed bids upon bid opening become publicly available, as did Flammann's incumbent contract, on January 8, 2001. For that reason alone, plaintiff's unit prices do not fit within Exemption 4 of FOIA, because publicly available information cannot meet part one of the National Parks "confidential" standard.

Id. (citations omitted).

37. *Id.* at 654 (citing the Trade Secrets Act, 18 U.S.C. § 1905 (2000)). Unit "price information does not fall under [the Trade Secrets Act] because overhead, profit margin, and other cost multipliers cannot be derived from unit prices." *Id*. (citing Acumenics Research & Tech. v. Dep't of Justice, 843 F.2d 800, 808 (4th Cir. 1988); Pac. Architects and Eng'rs, Inc. v. Dep't of State, 906 F.2d 1345, 1348 (9th Cir. 1990)).

38. *Flammann*, 53 Fed. Cl. at 654.

39. The court described the facts as "an imminent re-solicitation of a substantially similar contract covering largely the same period as those prices to be released on unperformed option years." *Id.* at 655.

basis for its decision, it ultimately held that in the interests of fairness, the contracting officer had a duty to withhold Flammann's contract prices, "particularly that of the future unperformed option years."[41] From the ensuing discussion of procurement integrity, the court appears to have accepted Facilma's assertion that the government's purpose in the resolicitation was a desire to lower contract prices.[42]

The essence of the court's decision is that contracting officers have a legal requirement to manage the procurement process in a fair and impartial manner; that the protection of the plaintiff's unit prices, though not confidential, is necessary to preserve the integrity of the contracting process; and that the maintenance of procurement integrity is more important than compliance with the FOIA's disclosure requirement; therefore, the contracting officer erred by effecting an otherwise lawful release of the plaintiff's unit price under the FOIA.

The logic behind the decision initially seems rational, but closer examination reveals its flaws. The weakest premise in the court's analysis is that the requirement to avoid an improper appearance trumps the requirement to release government records not exempt from disclosure under the FOIA. Moreover, very little precedent supports the decision.

The court's opinion appears to rest primarily on a line of reasoning adopted in *NFK Engineering, Inc. v. United States*.[43] In *NFK Engineering*, the court held that it was not irrational, arbitrary, or capricious for a contracting officer to disqualify a bidder based upon an appearance of impropriety.[44] In *NFK Engineering*, the contracting officer suspected that a former government employee—later employed by a government contractor—provided inside information or other improper assistance to the contractor. This information related to a project on which the employee had worked as a government expert.[45] These facts reflected a clear appearance of impropriety and the possibility of a violation of the law.

Observers who disagree with *Flammann*'s decision might argue that its facts are easily distinguished from those in *NFK Engineering*. In *NFK Engineering*, the court evaluated the contracting officer's judgment and response to what appeared to be an illegal act. In *Flammann*, the court evaluated the contracting officer's judgment and actions related to a legal act—the lawful and legally required disclosure of information under the FOIA. In *NFK Engineering*, the court ruled that it was not irrational, arbitrary, or capricious to disqualify a tainted contractor. In *Flammann*, the court ruled that the contracting officer should not have complied with Federal Acquisition Regulation (FAR) and FOIA disclosure requirements;[46] it also averred that compliance with the FAR and FOIA disclosure requirements was arbitrary and capricious, or otherwise violated the FAR requirement "to provide a level playing field for all bidders."[47]

The *Flammann* decision raises three concerns. First, the court's opinion appears to countenance a disregard for one of

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40. The court may have also contrasted the "arbitrary and capricious" nature of the government's release of the Flammann contract against the care with which the government would have protected its own cost estimates for the contracted work. In "outsourcing" the BOM services, the government could have submitted an in-house bid. The government's cost estimates and data related to its "most efficient organization" (MEO), however, would have been best protected under FOIA Exemption 5, which would permit the withholding of information the release of which would place the government at a competitive disadvantage.

41. *Flammann*, 53 Fed. Cl. at 655.

42. *Id.* at 650 n.10.

43. 805 F.2d 372 (Fed. Cir. 1986).

44. *Id*. at 378.

45. *Id.* at 374.

46. *Flammann*, 53 Fed. Cl. at 656.

> In answering the charge to the contracting officer to safeguard the interests of the United States in its contractual relationships by maintaining, in appearance and in fact, a fair and open competition not marred by fraud or favoritism, the contracting officer under the current solicitation had the authority to withhold plaintiff's unit prices.

Id.

47. *Id*.; *see also* GEN. SERVS. ADMIN. ET AL., FED. ACQUISITION REG. 1.602 (June 1997) [hereinafter FAR]**.** This provision of the FAR outlines the contracting officer's responsibilities:

> Contracting officers are responsible for ensuring performance of all necessary actions for effective contracting, ensuring compliance with the terms of the contract, and safeguarding the interests of the United States in its contractual relationships. In order to perform these responsibilities, contracting officers should be allowed wide latitude to exercise business judgment. Contracting officers shall—
> (a) Ensure that the requirements of 1.602-1(b) have been met, and that sufficient funds are available for obligation;
> (b) Ensure that contractors receive impartial, fair, and equitable treatment; and
> (c) Request and consider the advice of specialists in audit, law, engineering, transportation, and other fields, as appropriate.

Id.

the fundamental rules of statutory or legislative construction—that specific provisions within a rule supersede more general provisions. In this case, the court asserted that the contracting officer's "general" duty to ensure fairness[48] trumps that officer's duty to disclose the results of the earlier sealed bid.[49] This position subordinates the more specific provision of the regulation to the more general provision. While the court attempts to harmonize the two provisions,[50] it did not address the contradictory results that compliance with the separate provisions could create. Implicit in the court's equitable construction, however, is the assumption that compliance with either provision would result in the agency's non-compliance with the other provision.

Second, the court failed to note the distinction between statutory and regulatory requirements. *Flammann* highlights the differences between 5 U.S.C. § 552, a statute, and FAR section 14.402, a regulation. When there is a distinction between the requirements of statutes and regulations, traditional rules of construction require the court to follow the rule promulgated by the higher of the two authorities.[51] In *Flammann*, application of this maxim would have resulted in the court's dismissal of the plaintiff's complaint.[52]

Third, the absence of a clear factual analysis in the opinion and the inconsistencies discussed above suggest that the court misapplied the standard of review. The court clearly stated the standard to be applied in bid protest cases—an agency's decision "is to be set aside *only* if it is arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law."[53] The opinion also outlined both the court's limited ability to "second-guess" the agency[54] and the plaintiff's heavy burden to establish the "unreasonable" nature of the agency's actions.[55] After acknowledging that the agency has broad discretion,[56] however, the opinion's reasoning provides little evidence that the court gave the government's decision any deference. The opinion does not specifically state how the government's disclosure of Flammann's contract prices was arbitrary, capricious or unlawful. Instead, the court refers to the "*peculiar facts at bar.*"[57]

The court appears to advocate—but fails to address—that these peculiar facts could be analyzed under the often overlooked third prong of the *National Parks* test.[58] In earlier cases, courts have protected information submitted to the government when the disclosure "would hinder the agency in fulfilling its statutory mandate."[59] While the application of this third prong would have provided some interesting analysis, it is unlikely

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48. FAR, *supra* note 47, at 1.602-2.

49. *Flammann*, 53 Fed. Cl. at 656; *see* FAR, *supra* note 47, at 14.402.

50. *Flammann*, 53 Fed. Cl. at 656. The court asserted that the withholding of Flammann's unit prices under FAR section 1.602 would not "apparently" be

> contrary to the public access requirements of 48 CFR § 14.402(c), where "[e]xamination of bids by interested persons shall be permitted *if it does not interfere unduly with the conduct of government business*," that is to say, if public access does not unduly interfere with the prime directive of the contracting officer which is to "[e]nsure that contractors receive impartial, fair, and equitable treatment."

Id. (quoting 48 C.F.R. § 14.402(c) (2002)).

51. *See* Chevron U.S.A. v. Natural Res. Def. Council, 467 U.S. 837, 842-45 (1984).

52. The absence of any discussion of this issue may lead readers to assume that the court specifically avoided this analysis because its primary goal was to fashion an equitable remedy for a plaintiff, whom the court believed had been wronged either by the government's failure to exercise the contract option or by the "re-solicitation" of the contract so closely after it was originally let.

53. *Flammann*, 53 Fed. Cl. at 650-51 (citing 5 U.S.C. § 706(2)(A) (2000)).

54. *Id*. at 651. "Where an agency's decision is found to be reasonable, a court may not substitute its own judgment for that of the agency." *Id.* (citing Citizens to Preserve Overton Park v. Volpe, 401 U.S. 402, 416 (1971)).

55. *Id*. The plaintiff bears the burden to prove that the agency acted arbitrarily, capriciously, or unlawfully.

> Because it is well-settled that procurement officials are entitled to broad discretion in the evaluation of bids and in the application of procurement regulations, the plaintiff bears a heavy burden of showing, by clear and convincing evidence, either that (1) the agency decision-making process lacked a rational or reasonable basis, or (2) the procurement procedure involved a clear and prejudicial violation of applicable statutes or regulations.

Id. (citing Day & Zimmerman Serv., Inc. v. United States, 38 Fed. Cl. 591, 597 (1997)).

56. *Id*.

57. *Id*. at 654. The court's decision is even more remarkable because of its earlier conclusion that the plaintiff failed to "overcome the presumption of good faith on the part of the government." *Id.* at 649 n.7. It is difficult to escape the conclusion that the only arbitrary or capricious conduct the court can point to was the government's failure to provide a "coherent explanation" for its failure to exercise the Flammann contract option. *Id.* at 649.

58. Nat'l Parks and Conservation Assoc. v. Morton, 498 F.2d 765, 765 (D.C. Cir. 1974). In that case, the court "specifically left open the possibility of a third prong that would protect other governmental interests, such as compliance and program effectiveness." FOIA GUIDE, *supra* note 20, at 221.

that it would have supported the court's opinion that the government should have withheld Flammann's contract prices from SKE. Any analysis of the facts returns practitioners to the inescapable conclusion that the government cannot protect confidential information if that information has already been made public.

The facts at bar are not the only peculiar aspect of *Flammann*. While the court has wide latitude to fashion equitable remedies for injustices, it appears that the court did not fully embrace the FOIA's overarching purpose—to disclose information within the government's possession, unless it is clearly exempt from disclosure.[60] In this case, after identifying the competitive harm the release of contract prices caused,[61] the court acknowledged that the FAR makes sealed bid contract prices public,[62] explained that the "public availability" of sealed bid contract prices "logically nullifies any prospect of a confidentiality exemption" under the FOIA,[63] and then asserted that the contracting officer should have withheld the contract price information[64] in clear violation of the disclosure mandates of both the FAR and the FOIA.

The court's order also included a peculiar provision. The court predictably declared the re-solicitation to be null and void and enjoined the government from opening the affected bids or awarding a contract. The court also ordered the government to provide all bidders with copies of the contract unit prices that had previously been released to SKE.[65] The court then ordered the government to "level the playing field" by providing Flammann with the unit prices of all other bidders under its incumbent contract.[66] While this gesture initially seems to be fair, especially because Flammann had only sought its predecessor's unit prices,[67] it raises significant concerns. First, in relation to the unit prices of its predecessor, this order merely provided Flammann with another means of access to information that it had previously requested under the FOIA. Second, in relation to the unit prices of the unsuccessful bidders for the incumbent contract, the order merely provided Flammann with the information to which it had access at the time of the bid opening. While the court suggests that it is giving the plaintiff a benefit, it is difficult to identify just how this order assists Flammann in the next round of solicitations.

It is too early to speculate whether the government will appeal *Flammann* or merely assert that the court's holding is limited to the specific "peculiar facts" of that case. Consequently, contracting officers and attorneys may not be affected by the ruling. However, the case does "muddy the waters" in an already unsettled pool of unit price decisions. To paraphrase an old adage, the decision may prove that "peculiar facts" make peculiar law. Major Tuckey.

59. Pub. Citizen Health Research Group v. Nat'l Inst. of Health, 209 F. Supp. 2d 37, 45 (D.C. Cir. 2002).

60. "When a request is made, an agency may withhold a document, or portion thereof, only if the material at issue falls within one of the nine statutory exemptions found in [section] 552(b)." Maricopa Audubon Soc'y v. U.S. Forest Serv., 108 F.3d 1082, 1085 (9th Cir. 1997). The nine exemptions permit, but do not require, an agency to withhold a requested record. *See* 5 U.S.C. § 552 (2000).

61. *Flammann*, 53 Fed. Cl. at 652.

62. *Id.* at 653.

63. *Id.* at 654.

64. *Id.* at 655.

65. *Id.* at 657.

66. *Id.* at 657-58.

67. Flammann informed the court that "it submitted a FOIA request to the Army on 22 April 2002 to obtain the unit prices of its predecessor" and had not received those prices. *Id.* at 656 n.22.

Information Technology (IT)

Smart Cards[1]

Agencies are moving forward to procure smart cards for federal workers. The Department of Defense (DOD) Naval Inventory Control Point awarded four contracts to develop a common access card (CAC) software device to communicate with a microchip in the smart card.[2] An authentication certificate in the microchip verifies the identity of a computer network operator or provides digital signatures.[3] The CACs are another step to increase paperless contracting and electronic business.[4] The Defense Travel System in the Air Force also uses the CACs. Digital identification in the CACs is designed to certify travel orders and vouchers.[5] The General Services Administration (GSA) has also awarded a contract to develop a smart card for Department of Treasury employees.[6] The Electronic Treasury Enterprise Card (E-TREC) smart card "will provide access to buildings and computers as well as biometric identification and public key infrastructure."[7] Federal agencies are issuing smart cards to federal employees, but the idea to issue a smart card to all Americans is still a topic of debate.[8]

Moving Slowly Along

Last year's *Year in Review* reported on the Navy Marine Corps Intranet (NMCI) information technology outsourcing project.[9] The goal is to connect desktops and provide secure access to voice, data, and video communications for technology, maintenance, and help desk support. Only 21,000 employees are connected, although the current plan provides for connecting 100,000 employees. The $6.9 billion dollar project is moving "from the individual computer mentality to computing as an enterprise activity."[10] Enhanced computer security is built into the intranet project due to the interconnectivity of the system. The Navy plans to connect all 350,000 desktops and 200 networks to the NMCI by September 2003.[11]

IT Phone Home

The General Accounting Office (GAO) addressed numerous IT issues this year. The GAO addressed protection of critical IT infrastructure in two reports this past year. In October 2001, the GAO identified information-sharing practices to defend against cyber attacks.[12] In March 2002, the GAO recommended IT improvements for two agencies. It recommended that the Defense Logistics Agency strengthen its IT investment decisions,[13] and that the Defense Information Systems Agency improve IT investment planning and management controls.[14] In July 2002, the GAO recommended a comprehensive approach to enhance the nation's cyber infrastructures.[15]

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1. A recent article explained the concept of smart cards as follows:

> Smart cards are equipped with an electronic chip, magnetic strip and a barcode. They are used as an identification card and can grant physical access to defense facilities and electronically access computer networks. Smart cards can hold information about service members' inoculations, medical and dental records, finance allotments and other data.

Linda D. Kozaryn, *DoD to Implement Smart Card Program*, DefenseLINK (Oct. 27, 1999), *at* http://www.defenselink.mil/news/Oct1999/n102799_991027.html.

2. *Despite Obstacles, DOD Expands Common Access Card Use*, 44 GOV'T CONTRACTOR 30, ¶ 311 (Aug. 14, 2002).

3. *Id.*

4. The DOD pilot program reported the cards provided legally binding digital signatures, paperless business cost-savings, and network security. *Id.*

5. *Id.* at 5.

6. *GSA Task Order Contractor to Furnish Smart Cards to the Department of Treasury*, 44 GOV'T CONTRACTOR 31, ¶ 325 (Aug. 21, 2002).

7. *Id.* "The card serves as the individual identification key, or PKI for 'public key infrastructure.'" *See* Kozaryn, *supra* note 1, at 5.

8. Karen D. Schwartz, *Lawmakers, Agencies Study Smart Cards*, GovExec.com (Aug. 28, 2002), *at* http://www.govexec.com/dailyfed/0802/082802sl.htm.

9. "The NMCI is the Navy and Marine Corps [project] to outsource the technical, maintenance, and help desk support for over 350,000 desktops and 200 networks." Major John J. Siemietkowski et al., *Contract and Fiscal Law Developments of 2001—The Year in Review,* ARMY LAW., Jan./Feb. 2002, at 114 [hereinafter *2001 Year in Review*].

10. Karen Robb, *NMCI Starts Slower Than Planned*, DefenseNews (Sept. 28, 2002), *available at* http://www.defensenews.com.

11. *2001 Year in Review, supra* note 9, at 114.

12. GEN. ACCT. OFF., REP. NO. GAO-22-24, *Information Sharing: Practices That Can Benefit Critical Infrastructure Protection* (Oct. 15, 2001).

13. GEN. ACCT. OFF., REP. NO. GAO-02-314, *DLA Needs to Strengthen Its Investment Management Capability* (Mar. 15, 2002).

Finally, in September 2002, the GAO issued one of a series of reports reviewing the DOD's use of best practices in acquiring information technology health care systems.[16] In July 2002, the Director of the Office of Management and Budget (OMB) released a memo addressing IT concerns. The memo directed consolidating the Department of Homeland Security IT spending.[17] In addition, the OMB temporarily ceased IT infrastructure system developments and planned modernization efforts exceeding $500,000.[18] This delay will allow for the review and development of an integrated and universal IT system that best supports homeland security.[19]

IT Overlap?

The GSA hired an independent management and technology consulting firm, Accenture, to assess overlap between Federal Supply Service and Federal Technology Service IT contracts.[20] The report revealed that the GSA "has the right mix of products and services to serve federal customers," but also addressed inefficiencies in its performance.[21] Accenture recommended that the GSA "re-align the functional areas that focus on market research, marketing, customer planning and management, sales, service delivery, and contract development and maintenance."[22] The Accenture study affirmed that the recommendations should assist the GSA to improve its customer service.[23]

Electronic and Information Technology Accessibility

Last year's *Year in Review* reported on the requirement for federal departments and agencies to ensure that the electronic and information technology the government develops, procures, or maintains is accessible to federal employees and members of the public with disabilities.[24] On 27 June 2002, the Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council solicited comments regarding the need for guidance to promote more consistent and effective implementation of section 508.[25] Specifically, the councils requested that the respondents discuss the advantages and disadvantages of additional guidance, the form of the guidance,[26] and the focus of the types of IT purchases.[27] Major Davis.

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14. GEN. ACCT. OFF., REP. NO. GAO-02-50, *Information Technology: Defense Information Systems Agency Can Improve Investment Planning and Management Controls* (Mar. 15, 2002).

15. GEN. ACCT. OFF., REP. NO. GAO-02-474, *Critical Infrastructure Protection: Federal Efforts Require a More Coordinated and Comprehensive Approach for Protecting Information Systems* (July 15, 2002).

16. GEN. ACCT. OFF., REP. NO. GAO-02-345, *Information Technology: Greater Use of Best Practices Can Reduce Risks in Acquiring Defense Health Care System* (Sept. 15, 2002).

17. Memorandum from the Office of Management and Budget to the Heads of Selected Departments and Agencies, subject: Reducing Redundant IT Infrastructure Related to Homeland Security (July 19, 2002) (on file with author).

18. *Id.*

19. *Id.*

20. Findings and Recommendations, Accenture, Ltd., GSA Delivery of Best Value Information Technology Services to Federal Agencies, Analysis of FSS and FTS Structure and Services (Apr. 30, 2002) [hereinafter Accenture Study]. The study also reviewed overlapping offerings of telecommunications. *Id.*

21. *Id.* at 1. The Accenture study found:

1. Customers greatly value GSA services;
2. Industry partners also value GSA, though they see room to improve efficiencies in their interactions with GSA;
3. Overlap exists between FSS and FTS in the areas of IT sales and marketing and IT contract offerings; and
4. There is opportunity to expand GSA's delivery of best value in IT products and services.

Id.

22. *Id.* at 2.

23. *Id.*

24. *2001 Year in Review*, *supra* note 9, at 114.

25. Section 508 Contract Clause, 67 Fed. Reg. 43,523 (June 27, 2002) (to be codified at 48 C.F.R. pts. 39, 52).

26. The form of the guidance could be a FAR clause, a solicitation provision, other FAR coverage, or non-regulatory guidance.

27. 67 Fed. Reg. at 43,523.

Intellectual Property

During the past year, there were several noteworthy intellectual property cases in the federal courts and boards. All of these cases shared a common theme—contractors' claims that the government improperly took their intellectual property.

Statutory Prerequisites to Claim Damages—Infringement Must Occur in the United States

Outside the context of government contracts, if a patent owner believes someone is infringing on his patent, he may sue in any district court seeking compensation and injunctive relief to prevent further use.[1] If the government or a contractor working for the government is the alleged patent infringer, however, the patent owner's sole remedies are to file an administrative claim against the agency,[2] or to sue the government in the COFC, under 28 U.S.C. § 1498(a). In *Zoltek Corp. v. United States*,[3] the COFC held that the government was only liable under 28 U.S.C. § 1498 for patent infringements that occurred in the United States.[4]

In *Zoltek*, the government contracted with Lockheed Martin Corp. to design and build F-22 fighters. Lockheed, in turn, subcontracted with Nippon Carbon Co. and Ube Industries, two Japanese firms, to provide silicon carbide fiber materials. Zoltek Corp. owned a patent for silicon carbide fiber products, and alleged that these two Japanese firms infringed on Zoltek's patent by manufacturing the materials and delivering them to Lockheed Martin. Zoltek consequently sought compensation against the United States under 28 U.S.C. § 1498(a).[5] The government responded that 28 U.S.C. § 1498(c), which states that "[this] section shall not apply to any claim arising in a foreign country," precluded recovery where at least one element of the infringement occurred outside the United States.[6]

Despite the plain meaning of the statute, Zoltek argued that Congress intended the coverage of section 1498 to be co-extensive with the liability under 35 U.S.C. § 271, which defines what constitutes infringement when only private parties are involved.[7] If the coverage was not co-extensive, Zoltek argued, it would be without any remedy at all because section 1498(a) would bar a claim directly against Lockheed, and section 1498(c) would bar a claim against the United States.[8] Zoltek also pointed to several occasions in which Congress expressed a desire that infringement should not depend upon the identity of the infringer. The court agreed that this was Congress's expressed intent, but noted that even this express intent could not supersede the plain meaning of section 1498(c).[9]

Although the court found that section 1498(c) barred Zoltek's claim, it ordered the parties to file supplemental briefs addressing the question of whether the patent infringement constitutes a Fifth Amendment taking, and if so, whether section 1498(c) violates the requirement to provide just compensation.[10] Because the court also held in dicta that section 1498 literally only applies to manufacture or use—as opposed to sale or importation—of a patented invention,[11] the court's decision may mean that Zoltek can file suit directly against Lockheed and obtain an injunction preventing the importation of the Japanese firms' infringing products—an unpalatable outcome for the government.

Statutory Prerequisites to Claim Damages—The Statute of Limitations

Another COFC case applied the Fifth Amendment's takings clause to the Invention Secrecy Act.[12] When the U.S. Patent and Trademark Office (PTO) issues a patent, it discloses all the details necessary to replicate the underlying invention to the general public. This disclosure can have grave implications if

1. *See* 35 U.S.C. § 271 (2000).

2. *See* U.S. Dep't of Defense, Defense Federal Acquisition Reg. Supp. 227.7000 (21 Sept. 1999) [hereinafter DFARS].

3. 51 Fed. Cl. 829 (2002).

4. *Id.* at 839.

5. *Id.* at 829, 831.

6. *Id*. at 831-32 (quoting 28 U.S.C. § 1498(c) (2000)).

7. *Id.* at 832. The scope of 35 U.S.C. § 271 specifically includes importing a product from abroad that was made using an infringed patented process. *See* 35 U.S.C. § 271(a).

8. 51 Fed. Cl. at 832.

9. *Id.* at 837-38 (noting it could not fill the legislative gap in section 1498).

10. *Id.* at 838-39.

11. *Id.* at 838.

12. 15 U.S.C. §§ 181-188 (2000).

the invention has national security implications. The Invention Secrecy Act permits the Commissioner of Patents to place a "secrecy order" on a patent application if a government agency determines that publication or disclosure of the invention might be detrimental to the national security. If the Commissioner imposes a secrecy order, the PTO seals the patent application and prevents the issuance of a patent.[13]

The story of *Hornback v. United States*[14] began in August 1987, when the PTO notified Hornback that it was imposing a secrecy order on a patent application that he had filed. About a month later, the PTO issued Hornback a "Notice of Allowability," which stated that the PTO would have issued him a patent but for the secrecy order. The government did not rescind the secrecy order until April 1999, thus delaying Hornback's ability to obtain a patent on his invention. Hornback sued the government in January 1999, claiming that the government took his patent without just compensation in violation of the Fifth Amendment's Takings Clause.[15] The government contended that that COFC's six-year statute of limitations barred Hornback's claim.[16]

The government contended that Hornback's claim arose in August 1987, when the PTO initially imposed the secrecy order on Hornback's patent application. In contrast, Hornback argued that the claim did not arise until October 1993 because the government improperly classified the subject matter contained in the patent application in 1987 and did not correct that improper classification until 1993.[17] The court rejected Hornback's arguments, specifically noting that "if the government has taken property and has done so in a legally improper manner, it has committed two violations of the property owner's rights . . . giving rise to two separate causes of action."[18] The court went on to reason that the government's improper classification of the subject matter contained in Hornback's patent application did not affect his ability to file a claim for just compensation.[19]

Hornback alternatively argued that the "continuing claim" doctrine prevented his claim from being entirely time-barred.[20] The theory behind the continuing claim doctrine is that it is actually a series of distinct events rather than one single action by the defendant that wrongs the plaintiff. The Invention Secrecy Act prohibits the imposition of a secrecy order for more than one year, but it does permit the Patent Commissioner to renew the order for additional periods of up to one year if the agency that requested the secrecy order affirmatively determines that national interest requires the renewal.[21] Hornback contended each annual renewal of the secrecy order was a recurring individual wrong, and consequently, his action was not time-barred. The court held that the continuing claim doctrine did not apply to Hornback's case because the periodic renewals of the initial secrecy order were but "one act of imposition producing a harm that continued over a period of time."[22] The court held that Hornback's cause of action under the Fifth Amendment's Takings Clause was time-barred because he filed suit in 1999, more than six years after the imposition of the initial secrecy order.[23]

Contractors Must Mark Their Proprietary Information

In *General Atronics Corp.*,[24] the ASBCA ruled that a contractor's failure to precisely follow the regulatory requirements to mark its software with the appropriate rights legend before delivering it to the government resulted in the government having unlimited rights to that software. In 1992, the Navy issued a solicitation for the design and manufacture of data terminals. General Atronics Corp. (GAC) was the sole offeror. GAC's offer proposed several enhancements to the software and hard-

13. *See id.*; 35 U.S.C. § 181 (2000).

14. 52 Fed. Cl. 374 (2002).

15. *Id*. at 375-76 (citing U.S. CONST. amend. V, cl. 4).

16. *Id*. at 376.

17. 52 Fed. Cl. at 379.

18. *Id*. at 381 (citing *Del-Rio Drilling Programs, Inc. v. United States*, 146 F.3d 1358 (Fed. Cir. 1998), and noting that one cause of action would arise for just compensation and another for the improprieties committed in the course of the taking).

19. *Id*. at 388-89.

20. *Id*. at 378-79.

21. *Id*.

22. *Id.* at 379. The court did not fully explain its logic in reaching this conclusion; it is arguably incorrect because one could view each renewal of the secrecy order as a discrete event. *Id.*

23. *Id*. at 389.

24. ASBCA No. 49196, 02-1 BCA ¶ 31,798.

ware required by the solicitation. These enhancements would enable the data terminals to perform a greater number of applications and to work with two existing data terminals in the Navy's inventory. After negotiating for these enhancements, the Navy awarded GAC a $1,140,030 fixed-price contract for 194 data terminals. Shortly after the award, the parties began to dispute whether the contract required GAC to furnish only the hardware enhancements or both the hardware and software enhancements. GAC ultimately supplied the software enhancements under protest, but later submitted a claim for $203,684, which the government denied. Since the government's post-negotiation memorandum only discussed the hardware enhancements, the board sustained GAC's initial appeal.[25]

GAC and the Navy then began to dispute what rights the Navy had in the software enhancements. The solicitation and the Navy's resulting contract with GAC contained the "Rights in Technical Data and Computer Software (October 1988)" clause.[26] Among other things, this clause gives the government unlimited rights to any computer software that a contractor delivers to the government without a "Restricted Rights Legend."[27] It also prohibits a contractor from placing such a legend on any computer software until the government agrees to such restrictions in a license agreement, which must be incorporated into the contract between the contractor and the government.[28]

The cover page of GAC's proposal had a legend indicating that the proposal contained data that GAC considered to be proprietary and that the government could not disclose or use. Each page of the proposal also had a footer referencing the title page's legend. The software that GAC delivered as part of the data terminals, however, did not contain any restricted rights legend.[29] Although GAC attempted to remedy this omission by placing legends on the diskettes that it delivered to the Navy in 1995, the board ruled this was too late; the board held that by that time, the Navy had "gained unlimited rights" in the software.[30] The board also noted that the Navy never entered into a license agreement with GAC and highlighted the fact that GAC did not even propose to enter into a license agreement until long after it had started delivering the initial data terminals.[31]

Although GAC failed to comply with the regulatory requirements, it is difficult to fault GAC entirely. First, the regulations in this area are very complex and difficult to comprehend. Second, even though GAC did not place the appropriate marking on any of its delivered items, GAC did place notices on other hardware and data that indicated that they were proprietary. Most importantly, the regulations did not permit GAC to deliver the software with any restrictions on the government's rights to it unless GAC first obtained an advance license agreement that was made a part of the contract. Had the software been an initial requirement under the contract, it would not seem harsh to require GAC to comply with the regulatory requirements. Since the software enhancements were not part of the initial contract that GAC had with the government, however, it is troubling that the board was so unsympathetic to the contractor.

The last noteworthy case in this area is *Xerxe Group, Inc. v. United States*,[32] which applies a very strict and narrow interpretation of the marking requirements of the FAR provisions governing unsolicited proposals.[33] In *Xerxe*, an offeror submitted an unsolicited proposal[34] dealing with the privatization of utilities at Patrick Air Force Base. The government rejected Xerxe's proposal and subsequently published a Request for Information (RFI) that Xerxe claimed included proprietary information that the government had obtained from Xerxe's unsolicited proposal. Xerxe objected to the RFI and submitted a claim for $72 million in damages resulting from the government's alleged violation of the FAR's confidentiality provisions and improper dissemination of its proprietary information to the general public. In November 2000, the COFC, in an unreported decision, held that Xerxe's failure to comply with the requirements of FAR 15.609(b) "vitiated any protection against disclosure."[35] Xerxe appealed that ruling to the CAFC.[36]

25. *Id*. at 157,066.

26. DFARS, *supra* note 2, at 252.227-7013.

27. *Id*. at 252.227-7013(c).

28. *Id*.

29. *General Atronics*, 94-3 BCA ¶ 27,112, at 157,066-67.

30. *Id*. at 157,068. Interestingly, the board did not expressly address DFARS 227.7203-10(c), which allows a contractor to "request permission" to insert an inadvertently omitted legend. As previously discussed, the board indicated in a footnote that GAC had submitted software with restrictive legends, but followed this with a note that the contracting officer "took exception" to the markings. *Id*. at 157,068 n.2.

31. *Id*.

32. 278 F.3d 1357 (Fed. Cir. 2002).

33. General Servs. Admin. et al., Federal Acquisition Reg. 15.609 (Sept. 1997) [hereinafter FAR].

34. An "unsolicited proposal" is a proposal for a new or innovative idea that is not submitted in response to a government solicitation or announcement. FAR, *supra* note 33, at 2.101; *see also id*. subpt. 15.6.

The FAR requires anyone submitting an unsolicited proposal containing proprietary information to mark the title page to the proposal with a specific legend that places the government on notice that it must protect the proprietary information from disclosure.[37] It also requires the submitter to mark each page of the proposal with a different legend that cross-references the one placed on the title page to the proposal.[38] If these two steps are done properly, government personnel are prohibited from disclosing the marked information.[39] Unfortunately, the contractor in *Xerxe* only placed the required legend on the offer's title page. The CAFC found the lack of any marking on the individual pages within the proposal to be dispositive and upheld the lower court's opinion.[40]

The CAFC failed to address several other FAR provisions that would argue against the government's ability to use the unmarked information in Xerxe's proposal. In addition to prohibiting the disclosure of properly marked information, the FAR also prohibits government personnel from using "any data, concept, idea or other part of an unsolicited proposal" in a solicitation or negotiation with any other firm.[41] This prohibition does not depend upon whether the provider appropriately marked the information. If the government intends to have any non-government personnel evaluate an unsolicited proposal, the FAR requires the government to obtain the offeror's written permission before it may release the proposal to those individuals. Again, this requirement applies regardless of whether the proposal contains any markings indicating that it contains proprietary information.[42] Before *Xerxe*, a contractor—particularly one with little government contracting experience—could reasonably read FAR subpart 15.6 to mean that the government could not disseminate information from an unsolicited proposal outside the government, regardless of whether the information was properly marked. Like *General Atronics Corp.*, *Xerxe* established an exacting obligation on contractors to comply with the precise marking requirements created by confusing and extensive regulations. Major Sharp.

35. *Xerxe*, 278 F.3d at 1358 (citing Xerxe Group, Inc. v. United States, No. 99-924-C (Ct. Fed. Cl. Nov. 30, 2000)).

36. *Id*.

37. *See* FAR, *supra* note 33, at 15.609(a).

38. *Id*. at 15.609(b).

39. *Id*. at 15.608(b).

40. 278 F.3d at 1359-60.

41. FAR, *supra* note 33, at 15.608(a).

42. *Id*. at 15.609(h).

Non-FAR Transactions

Although neither case law nor legislation enacted during the past year dealt with contracts falling outside the purview of the Federal Acquisition Regulation (FAR),[1] several agencies issued proposed and final rules in the area. In addition, both houses of Congress introduced multiple bills that would have extended Other Transaction authority to either the Homeland Security Department[2] or to all civilian agencies.[3] If this past year is any indication of what the future has in store for non-FAR transactions, it appears that agencies will continue to rely on them to an increasing degree, but at the same time, the government will subject them to greater scrutiny and more regulation.

DOD Proposes Greater Flexibility in Technology Investment Agreements

Beginning in 1947, Congress gave the Department of Defense (DOD) the authority to engage in research projects using contractual methods that did not have to comply with the normal statutory and regulatory government contract rules. First, Congress enacted 10 U.S.C. § 2358,[4] which gave the DOD the authority to engage in research efforts through the use of either a Cooperative Agreement or a grant. In 1989, Congress enacted 10 U.S.C. § 2371,[5] giving the DOD the authority to use "Other Transactions"[6] for such research. Neither of these authorities permits the DOD to acquire an actual product; they merely allow the DOD to make investments to stimulate research in scientific fields of interest to DOD, with the expectation that the DOD may actually use the research in one or more of its weapon systems.[7]

To implement these statutory authorities, the DOD promulgated the DOD Grant and Agreement Regulations (DODGARs). One of the contractual vehicles discussed in this regulation is a Technology Investment Agreement (TIA), which could be either a Cooperative Agreement or an Other Transaction.[8]

Last year, the DOD proposed a rule that would add a new part 37 to the DODGARs.[9] The proposed rule would provide guidance to agreements officers on the policies and procedures concerning the award and administration of TIAs. The proposed rule, which is written in a question-and-answer format, would also make some minor changes to existing parts 21, 22, 32, and 34 of the DODGARs. One of the major purposes for the proposed revision is to ensure that agreements officers are more aware of the flexibility they have in negotiating and awarding TIAs, potentially enabling the DOD to attract nontraditional defense contractors to conduct research work for it.[10]

GAO's Access to 845 Agreement Records

As discussed above, Congress has given the DOD limited authority to acquire actual quantities of end items, as opposed to just stimulating research using an Other Transaction. This sort of transaction is alternatively referred to as either an Other Transaction for Prototype or an 845 Agreement. In Section 801 of the National Defense Authorization Act for Fiscal Year 2000,[11] Congress required the DOD to include a clause in every 845 Agreement involving payments of over $5 million; this clause gives the GAO the ability to examine the records of any of the parties involved. Congress allowed for certain exceptions to this requirement, most notably, exempting any party

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1. Commonly called "non-FAR Transactions."

2. *See* H.R. 5005, 107th Cong. (2002); S. 2794, 107th Cong. (2002).

3. *See* H.R. 3426, 107th Cong. (2001); S. 1780, 107th Cong. (2001); H.R. 4694, 107th Cong. (2002) (restricting this authority to situations when the research facilitates defending or recovering from terrorism, or from a nuclear, biological, chemical, or radiological attack).

4. Pub. L. No. 85-599, 72 Stat. 520 (1947).

5. Pub. L. No. 101-189, 103 Stat. 1403 (1989).

6. 10 U.S.C. § 2371 (2000). The phrase "Other Transaction" has become the term of art for instruments the statute refers to as "transactions (other than contracts, cooperative agreements, and grants)." *Id*.

7. In 1993, Congress also gave the DOD the authority to enter into "Other Transactions," in which the DOD acquires limited amounts of prototype items rather than just the underlying research. This sort of Other Transaction is alternatively referred to as an "other transaction for prototype" or an "845 Agreement" because it arose out of section 845 of the National Defense Authorization Act for Fiscal Year 1994. *See* Pub. L. No. 103-160, § 845, 107 Stat. 1547, 1721 (1993).

8. U.S. Dep't of Defense, Reg. 210.6-R, DOD Grant and Agreement Regulations (13 Apr. 1998), *available at* http://www.dtic.mil/whs/directives/corres/html/32106r.htm.

9. *See* DOD Grant and Agreement Regulations, 67 Fed. Reg. 21,486 (proposed Apr. 30, 2002) (to be codified at 32 C.F.R. pt. 37).

10. *Id.*

11. Pub. L. No. 106-65, § 8801, 113 Stat. 512, 700 (1999).

who had not entered into an Other Transaction that provided audit access during the preceding year.[12]

In section 804 of the National Defense Authorization Act for Fiscal Year 2001,[13] Congress carved out an additional exception to the mandate to attain record access. Congress indicated that if the party to the 845 Agreement had only done business with the government during the past year via an Other Transaction or a Cooperative Agreement, then the mandated clause in the current 845 Agreement would only need to grant the GAO the same access rights that the previous agreement permitted. This past year, the DOD issued a final rule incorporating the congressional mandate discussed above.[14]

Restrictions on the Use of 845 Agreements

In addition to expanding the exceptions to the GAO's record access, the National Defense Authorization Act for Fiscal Year 2001 limited the DOD's ability to enter into 845 Agreements.[15] Congress authorized the DOD to use 845 Agreements only under three circumstances: (1) where a non-traditional defense contractor participates to a significant extent; (2) where one or more non-federal government parties pays at least one-third of the funds for the project; or (3) where the agency's senior procurement executive makes a determination that exceptional circumstances exist, such that the 845 Agreement allows them to accomplish what would not be feasible under a contract. Congress also provided a statutory definition for "nontraditional defense contractor."[16] Last year, the DOD issued a proposed rule that would implement these statutory requirements.[17] This proposed rule also called for the inclusion of clauses granting the DOD audit rights in any agreement relying upon the "at least one-third private funding" justification, or any agreement where payment was based upon that party's costs.[18] In response to multiple comments regarding the audit rights provisions,[19] the DOD ultimately decided to issue a final rule that addressed only the restrictions on using 845 Agreements.[20] A separately issued memorandum indicates that the DOD eventually plans to issue an additional rule covering the audit provisions.[21]

GAO Report Calls for Changes in 845 Agreement Reporting Requirements

Currently, the DOD is required to submit an annual report to Congress covering its 845 Agreements.[22] In a recently issued report, the GAO commended the DOD on its implementation of the 845 Agreement authority to date, but also called for the DOD to provide better, more straightforward information regarding nontraditional contractor involvement in its annual reports.[23] The GAO specifically called for a summary table that indicated the number of nontraditional contractors that the DOD enticed to do business with it through the use of an 845 Agreement.[24] It also recommended that the DOD provide, as

12. *Id.*

13. Pub. L. No. 106-398, § 804, 114 Stat. 1654, 1654A-206 (2000).

14. *See* Transactions Other than Contracts, Grants, or Cooperative Agreements for Prototype Projects, 66 Fed. Reg. 57,381 (Nov. 15, 2001).

15. Pub. L. No. 106-398, § 803, 114 Stat. 1654, 1654A-205 (2000).

16. *Id*. at 1654A-205-06. This law defines a "nontraditional defense contractor" as follows:

> [A]n entity that has not, for a period of at least one year prior to the date that a transaction (other than a contract, grant, or cooperative agreement) for a prototype project under the authority of this section is entered into, or performed with respect to—(1) any contract that is subject to full coverage under the cost accounting standards prescribed pursuant to section 26 of the Office of Federal Procurement Policy Act (41 U.S.C. 422) and the regulations implementing such section; or (2) any other contract in excess of $500,000 to carry out prototype projects or to perform basic, applied, or advanced research projects for a Federal agency, that is subject to the Federal Acquisition Regulation.

Id.

17. *See* Transactions Other than Contracts, Grants, or Cooperative Agreements for Prototype Projects, 66 Fed. Reg. 57,422 (Nov. 21, 2001).

18. *Id*. at 58,423.

19. *See, e.g.*, *Other Transactions: Bar Group, Dual-Use Commercial Firms Urge DOD to Withdraw OT Audit Rights Proposal*, 77 BNA FED. CONT. REP. 95 (JAN. 31, 2002).

20. *See* Transactions Other than Contracts, Grants, or Cooperative Agreements for Prototype Projects, 67 Fed. Reg. 54,955 (Aug. 27, 2002).

21. *See* Memorandum, Director of Defense Procurement, to the Directors of Defense Agencies, and Deputy Assistant Service Secretaries, subject: Clarification Regarding Conditions on Use of "Other Transaction" Agreements for Prototype Projects (Aug. 27, 2002), *available at* http://www.acq.osd.mil/dp/dsps/ot/dpmemo8272002.pdf.

22. *See* 10 U.S.C. § 2371(h) (2000).

23. *See* GEN. ACCT. OFF., REP. NO. GAO-03-150, *DOD Has Implemented Section 845 Recommendations but Reporting Can Be Enhanced* (Oct. 9, 2002).

part of its submission to Congress, an assessment of the benefits ensuing from projects completed during the preceding year.[25]

SBIR Changes

In 1982, Congress enacted the Small Business Innovation Development Act (SBIDA).[26] The Act created the Small Business Innovative Research (SBIR) Program, an effort designed to increase the role that small business concerns could play in federally funded research and development. This program authorizes certain designated federal agencies to award "phased" contracts not governed by the FAR in order to promote scientific and technological innovation in fields that are of interest to the respective agencies.[27] Although the SBIDA initially set an expiration date of 1 October 1988 for the Program,[28] Congress has subsequently reauthorized it several times. The most recent reauthorization was in 2000;[29] along with it came several statutorily prescribed changes to the SBIR Program. To implement these prescribed changes, the Small Business Administration has issued a revised policy directive that applies to all agencies involved in the program.[30]

Some of the more important changes required in the 2000 legislation included: (1) requiring the SBA to clarify that the government's rights in data apply to data generated in any of the three contract phases;[31] (2) creating a database which would enable the public to search through information related to past SBIR awards;[32] (3) requiring an applicant for a Phase II award to describe their commercialization plan; (4) requiring an agency to report to the SBA whenever it determined that a Phase III award would not be practicable; and (5) creating the Federal and State Technology (FAST) Partnership, which adds state and local entities to the SBIR process.[33] In addition to providing a copy of the revised policy directive, the Federal Register notice does an excellent job of providing a section-by-section analysis of the changes and also discusses the public comments.[34]

Grant Me Some Improvements!

In 1999, Congress enacted the Federal Financial Assistance Management Improvement Act.[35] The purpose of the Act was to streamline and improve the effectiveness of the various federal grant programs. The Act noted that there were over 600 grant programs in existence, and that the lack of uniformity among these programs was creating inefficiencies. Consequently, Congress directed the Office of Management and Budget (OMB) to streamline the regulations dealing with grants and to establish standard ways to award and administer them.[36]

In response to this congressional directive, the OMB issued five notices last year concerning revisions to its old guidance, as well as new guidance that would streamline and standardize the award and administration of federal grants. First, the OMB proposed to amend *OMB Circular A-133*[37] by increasing the thresholds that the grantee would have to meet before being subject to an audit.[38] The OMB also proposed to amend OMB Circulars A-21,[39] A-87,[40] and A-122.[41] Currently, there are occasional differences between how each of these three circulars describes or defines cost items. There is also a lack of con-

24. *See id*. at 9 (indicating that the DOD non-concurred with this recommendation in agency comments it sent to the GAO).

25. *Id*. at 9-10 (noting that the DOD concurred with this recommendation, but also indicating that it would provide such information on an *ad hoc*, as opposed to a regular, basis).

26. Pub. L. No. 97-219, 96 Stat. 217 (1982).

27. 96 Stat. at 218.

28. 96 Stat. at 221.

29. *See* Pub. L. No. 106-554, 114 Stat. 2763A-668 (2000) (extending the SBIR Program through 30 September 2008).

30. *See* Small Business Innovation Research Policy Directive, 67 Fed. Reg. 60,072 (Sept. 24, 2002).

31. 114 Stat. at 2763A-673.

32. *Id*. at 2763A-670-71.

33. *Id*. at 2763A-674.

34. *See* Small Business Innovation Research Policy Directive, 67 Fed. Reg. 60,072 (Sept. 24, 2002).

35. Pub. L. No. 106-107, 113 Stat. 1486 (1999).

36. *Id.* at 1488.

37. U.S. Office of Mgmt. and Budget, Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations (June 24, 1997).

38. *See* Audits of States, Local Governments, and Non-Profit Organizations, 67 Fed. Reg. 52,545 (Aug. 12, 2002).

sistency in cost policy between these circulars. The proposed revisions do away with these inconsistencies.[42]

One of the OMB notices deals with a proposal to issue a new policy mandating a standardized format for publicizing agency announcements.[43] A second OMB notice proposes to standardize the data to include in synopses sent to FedBizOpps.[44] Both of these efforts would enable potential grant applicants to screen agency announcements more quickly, to determine if the proposed funding opportunity deals with an area that interests them. The OMB also issued a notice concerning its decision not to change OMB Circular A-110.[45] The OMB had previously planned to revise this circular so that grantees having multiple grants with an agency could request payments on a "pooled" rather than a grant-by-grant basis. Ultimately, the OMB decided not to make this change because of the disparity in public comments on the proposal.[46]

NASA Grant and Agreement Revisions

In section 431 of the Departments of Veterans Affairs and Housing and Urban Development and Independent Agencies Appropriations Act for Fiscal Year 1999,[47] Congress authorized the National Aeronautics and Space Administration (NASA) to indemnify anyone that develops an "experimental aerospace vehicle" under a Cooperative Agreement with NASA. In section 319 of the NASA Authorization Act for Fiscal Year 2000,[48] Congress announced that it believed that any non-profit recipient of a grant or Cooperative Agreement should purchase only American-made products when spending that assistance. A final NASA rule implements these statutes, making changes to both its "Grant and Cooperative Agreements" regulations and its "Cooperative Agreements with Commercial Firms" regulations. This final rule also made some changes to both sets of regulations dealing with publishing requirements and the evaluation and selection of competing firms.[49] Major Sharp.

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39. U.S. Office of Mgmt. and Budget, Circular A-21, Cost Principles for Educational Institutions (Aug. 8, 2000).

40. U.S. Office of Mgmt. and Budget, Circular A-87, Cost Principles for State, Local and Indian Tribal Governments (Aug. 29, 1997).

41. U.S. Office of Mgmt. and Budget, Circular A-122, Cost Principles for Non-Profit Organizations (June 1, 1998).

42. *See* Cost Principles for Educational Institutions, for State, Local and Indian Tribal Governments and for Non-Profit Organizations, 67 Fed. Reg. 52,558 (proposed Aug. 12, 2002), *available at* http://www.whitehouse.gov/omb/fedreg/cost_principle_nprm_table.pdf) (citing a chart of the inconsistencies and proposed changes).

43. Office of Federal Financial Management Policy Directive on Financial Assistance Program Announcements, 67 Fed. Reg. 52,548 (proposed Aug. 12, 2002).

44. Standard Data Elements for Electronically Posting Synopses of Federal Agencies' Financial Assistance Program Announcements at FedBizOpps, 67 Fed. Reg. 52,554 (proposed Aug. 12, 2002).

45. U.S. Office of Mgmt. and Budget, Circular A-110, Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations (Sept. 30, 1999).

46. *See* U.S. Office of Mgmt. and Budget, Circular A-110, Uniform Administrative Requirements for Grants and Agreements with Institutions of Higher Education, Hospitals, and Other Non-Profit Organizations, 67 Fed. Reg. 52,547 (Aug. 12, 2002).

47. Pub. L. No. 105-276, § 431, 112 Stat. 2461, 2513-16 (1998).

48. Pub. L. No. 106-391, § 319, 114 Stat. 1577, 1597 (2000).

49. *See* NASA Grant and Cooperative Agreement Handbook—Rewrite of Section D—Cooperative Agreements with Commercial Firms and Implementation of Section 319 of Public Law 106-391, Buy American Encouragement, 67 Fed. Reg. 45,790 (July 10, 2002) (codified at 14 C.F.R. pts. 1260, 1274).

Payment and Collection

Not So Fast There, Buddy!

In a memorandum issued on 30 May 2002, the Director of Defense Procurement, Ms. Deidre Lee, cautioned Department of Defense (DOD) paying officials about using fast payment procedures without first meeting all of the requirements of Federal Acquisition Regulation (FAR) section 13.402.[1] Ms. Lee noted that "[t]he fast payment procedure allows payment under limited conditions to a contractor prior to the government's verification that supplies have been received and accepted."[2] Federal Acquisition Regulation section 13.402 provides six conditions, however, which must be present before paying officials can use the fast payment procedures.[3]

The catalyst for Ms. Lee's caution was a Defense Finance and Accounting Service (DFAS) observation that paying offices had used fast payment procedures when there was no geographical separation or lack of adequate communications facilities that made it impractical to make timely payment based on evidence of government acceptance. The DFAS also observed that the receiving activities frequently would not forward it a copy of the receiving report as a follow-up to a fast payment.[4] Ms. Lee stated in her memorandum that "[i]n today's e-business environment, use of fast payment procedures should be employed only when payment must be made inside the United States for deliveries made outside the United States."[5] Ms. Lee ordered DOD components to review their fast payment procedures and ensure they "have the necessary internal controls in place and are complying with all the requirements of FAR 13.402."[6]

Garbage In, Garbage Out—Contracting Officers Should Structure Payment Terms Properly for Correct and Timely Payment

A couple of weeks after issuing the fast payment procedures memo, Ms. Lee issued another memorandum, this one emphasizing that contracting activities need to input payment and delivery information into automated systems properly, so that contractors receive correct and timely payments.[7] Ms. Lee's 11 June 2002 memo reminded DOD components of the following contract formation issues that may cause delays in payment:

> (1) CLIN [Contract Line Item Number] structure inconsistent with contractors' shipping [and] billing methods;
>
> (2) Unit pricing by lot when contractor[s] could deliver separately priced items as partial shipments; and

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1. Memorandum, Deidre A. Lee, Director, Defense Procurement, to Directors of Defense Agencies, Deputy Assistant Secretary of the Army (Procurement), Deputy for Acquisition and Business Management, ASN (RD&A)/ABM, Deputy Assistant Secretary of the Air Force (Contracting), SAF/AQC, Executive Director, Logistics Policy & Acquisition Management (DLA), subject: Fast Payment Procedures (30 May 2002) [hereinafter Lee FPP Memo] (citing GENERAL SERVS. ADMIN. ET AL., FEDERAL ACQUISITION REG. 13.402 (July 2002) [hereinafter FAR]).

2. Lee FPP Memo, *supra* note 1. Ms. Lee defined "identified fast payment procedures" as the FAR describes them. *See* FAR, *supra* note 1, at 13.401(a).

3. The FAR lists six conditions that paying officials must meet before they use the fast payment procedures:

> (1) the individual purchasing instruments does not exceed $25,000;
> (2) deliveries of supplies are to occur at locations where there is both a geographical separation and a lack of adequate communications facilities between the Government receiving and disbursing activities that will make it impractical to make timely payment;
> (3) title to the supplies passes to the Government upon delivery to a post office or common carrier for mailing or shipment to destination, or, upon receipt by the Government if the shipment is by means other than Postal Service or common carrier;
> (4) the supplier agrees to replace, repair, or correct supplies not received at destination, damaged in transit, or not conforming to purchase requirements;
> (5) the purchasing instrument is a firm-fixed-price contract, a purchase order, or a delivery order for supplies; and
> (6) a system is in place to ensure documentation of evidence of contractor performance under fast payment purchases, timely feedback to the contracting officer in case of contractor deficiencies, and identification of suppliers that have a current history of abusing the fast payment procedure.

FAR, *supra* note 1, at 13.402.

4. *See* Lee FPP Memo, *supra* note 1.

5. *Id.*

6. *Id.*

7. Memorandum, Deidre A. Lee, Director, Defense Procurement, to Directors of Defense Agencies, Deputy for Acquisition and Business Management, ASN (RD&A), Deputy Assistant Secretary of the Air Force (Contracting), SAF/AQC, Deputy Assistant Secretary of the Army (Procurement) ASA(ALT), Executive Director, Logistics Policy & Acquisition Management (DLA), subject: Contract Payment (11 June 2002) [hereinafter Lee Payment Memo].

> (3) Requirement description by reference to the contractor's proposal when receiving, accepting and paying activities may not have that information.[8]

Ms. Lee placed special emphasis on contracts with commercial suppliers inexperienced with government business processes:

> We must ensure that our contracts are written clearly with all the information necessary for receipt, acceptance, and payment (including the military address for delivery) so that commercial suppliers receive timely payment and are more likely to continue to do business with the Department.[9]

Ms. Lee also advised contracting officers to consider recently added GSA schedule items on the DOD E-Mall because commercial suppliers may find this automated ordering procedure more familiar than the traditional purchase order system.[10]

From a DOD efficiency standpoint, Ms. Lee noted that the DOD "cannot afford to use scarce human resources to manually reconcile inconsistent information, or to search for missing information."[11]

"Count Your Change!" GAO Releases Yet Another Report Saying That DOD Overpayments Continue

Department of Defense overpayment problems are nothing new for the GAO, which initially reported on DOD contractor overpayments in 1994.[12] As last year's *Year in Review* noted, the GAO recently issued several more reports criticizing government payment and collection systems.[13] In May 2002, the GAO released yet another report indicating that DOD officials continue to make overpayments on contracts.[14] While the GAO noted that the DOD had begun several initiatives to reduce overpayments, it also reported as follows:

> [The DOD] still does not yet have basic accounting control over contractor debt and underpayments because its procedures and practices do not fully meet federal accounting standards and federal financial system requirements for the recording of accounts receivable and liabilities. As a result, DOD managers do not have important information for effective financial management, such as ensuring that contractor debt is promptly collected.[15]

Overall, DFAS Columbus records revealed that the DOD made approximately $488 million in overpayments during fiscal year (FY) 2001.[16]

"We Are Here to Help!" Congress Requires Agency Programs for Identifying Payment Errors

Last year's *Year in Review* noted that Representative Dan Burton introduced the Erroneous Payments Recovery Act of 2001 to address government overpayments.[17] This legislation eventually gave birth to section 831 of the National Defense Authorization Act for FY 2002.[18] Section 831 amended Title 31 of the U.S. Code[19] to require that the head of each executive agency with contracts totaling over $500 million in a fiscal year

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8. *Id*.

9. *Id*.

10. *Id*.

11. *Id*.

12. GEN. ACCT. OFF., REPT. NO. GAO/NSAID-94-106, *DOD Procurement: Millions in Overpayments Returned by DOD Contractors* (Mar. 14, 1994).

13. *See* Major John J. Siemietkowski et al., *Contract and Fiscal Law Developments of 2001—The Year in Review*, ARMY LAW., Jan./Feb. 2002, at 119 [hereinafter *2001 Year in Review*].

14. GEN. ACCT. OFF., REP. NO. GAO-02-635, *DOD Contract Management: Overpayments Continue and Management and Accounting Issues Remain* (May 30, 2002).

15. *Id*. at 3.

16. *Id*. at 2.

17. *See 2001 Year in Review*, *supra* note 13, at 119.

18. *See* National Defense Authorization Act for Fiscal Year 2002, Pub. L. No. 107-107, § 831, 115 Stat. 1012, 1186 (2001). On 6 June 2002, Representative Stephen Horn (R-Cal.) introduced a bill, to provide for federal agency reduction of improper payments. The proposed act would not only require each agency to annually identify all programs and activities that may be susceptible to significant improper payments, the agency must also subsequently estimate the amount of improper payments and report that estimate in their budget submissions and annual program performance reports. H.R. 4878, 107th Cong. (2002).

establish a cost-effective program for identifying payment errors and for the recovery of overpayments.[20] Major Kuhn.

19. *See* 31 U.S.C. §§ 3561-3567 (2000).

20. *Id*.. § 3561(a).

Performance-Based Service Contracting

New Rules on Performance-Based Service Contracting

In last year's *Year in Review,* the authors noted a change to the Army Federal Acquisition Regulation Supplement (AFARS)[1] that required all service contracts to be performance-based and fixed-price.[2] Just seven months later, the Army deleted this newly created provision entirely when it issued Version 4 of the AFARS.[3] All practitioners, including those in the Army, obviously must still follow the relevant Federal Acquisition Regulation (FAR) guidance regarding performance-based service contracts (PBSCs). In that regard, the General Accounting Office (GAO) issued a final rule last year,[4] implementing the preference for PBSCs established in section 821 of the Floyd D. Spence National Defense Authorization Act for Fiscal Year 2001.[5] The final rule adopted the previous year's interim rule guidance on PBSCs,[6] but also amended FAR section 7.105(b)(4) "to clarify that contracting officers must provide a rationale if a performance-based contract will not be used or if a performance-based contract for services is contemplated on other than a firm-fixed price basis (see [FAR sections] 37.102(a) and 16.505(a)(3))."[7]

Additionally, on 6 December 2001, the Department of Defense (DOD) issued an interim amendment to the Defense Federal Acquisition Regulation Supplement (DFARS), adding section 212.102, which allows the DOD to treat certain PBSCs and task orders as contracts for the procurement of commercial items.[8] The rule permits contracting officers to use the commercial item acquisition procedures under FAR part 12 for firm fixed-price PBSCs or task orders with a value of $5 million or less, if the contract satisfies certain conditions. First, the contract or task order must define each specific task to be performed in "measurable, mission-related terms," and "identify the specific end products or output to be achieved for each task."[9] The contractor also must provide "similar services at the same time to the general public under terms and conditions similar to those in the contract," and the agency must not use the procedures in FAR subpart 13.5, Test Program for Certain Commercial Items.[10] Noting that contracts under FAR part 12 incorporate the clauses at FAR sections 52.212-4 and 52.212-5, the interim rule notice advises contracting officers of the potential need to modify the inspection and acceptance provisions at section 52.212-4(a) to protect the government's interests adequately. The notice informs agencies, for example, that they must include commercial remedies such as the extension of contract performance or the right to reduce contract price when reperformance cannot correct defects in the services provided.[11]

The DOD finalized the interim rule with minor revisions on 25 October 2002.[12] The final rule adds the phrase "or task order" to the end of the requirement that the contractor offer "similar services at the same time to the general public under terms and conditions similar to those in the contract."[13] Because the word "tailor" is consistent with terminology used elsewhere in FAR part 12, the new rule also adopts its use instead of the term "modify," in conjunction with possible

1. U.S. DEP'T OF ARMY, ARMY FEDERAL ACQUISITION REG. SUPP. (Jan. 25, 2002) [hereinafter AFARS].

2. Major John J. Siemietkowski et al., *Contract and Fiscal Law Developments of 2001—The Year in Review,* ARMY LAW., Jan./Feb. 2002, at 14.

3. *See* AFARS, *supra* note 1. Before this deletion, a January 2002 interim change exempted service contracts related to architecture and engineering, construction, certain supply contracts, and A-76 studies from the general policy. *Id.*

4. Federal Acquisition Regulation; Preference for Performance-Based Contracting, 67 Fed. Reg. 21,532 (Apr. 30, 2002) (to be codified at 48 C.F.R. pts. 2, 7, and 37).

5. Pub. L. No. 106-398, § 821, 114 Stat. 1654, 1654A-217 (2000).

6. Federal Acquisition Regulation; Preference for Performance-Based Contracting, 66 Fed. Reg. 22,082 (May 2, 2001). The rule defined performance-based contracting as "structuring all aspects of an acquisition around the purpose of the work to be performed with the contract requirement set forth in clear, specific, and objective terms with measurable outcomes." GENERAL SERVS. ADMIN. ET AL., FEDERAL ACQUISITION REG. 2.101(b) (Sept. 2001) [hereinafter FAR]. The rule also stated that agencies must use performance-based contracting methods "to the maximum extent practicable," except for architect-engineer, construction, and utility services and services incidental to supply contracts. *Id.* at 37.102.

7. 67 Fed. Reg. at 21,532.

8. Defense Federal Acquisition Regulation Supplement; Performance-Based Contracting Using Federal Acquisition Regulation Part 12 Procedures, 66 Fed. Reg. 63,335 (Dec. 6, 2001) (implementing section 821(b) of the Floyd D. Spence National Defense Authorization Act for Fiscal Year 2001, Pub. L. No. 106-398, § 821, 114 Stat. 1654, 1654A-218 (2000)).

9. *Id*.

10. *Id*.

11. *Id*. at 63,336.

12. Defense Federal Acquisition Regulation Supplement; Performance-Based Contracting Using Federal Acquisition Regulation Part 12 Procedures, 67 Fed. Reg. 65,512 (Oct. 25, 2002) (to be codified at 48 C.F.R. pts. 212, 226, and 237).

13. *Id*. at 65,513.

changes to applicable FAR clauses.[14] More significantly, the final rule also amends section 226.104 to clarify that "there is no restriction on use of the clause at [section] 252.226-7001 [Utilization of Indian Organizations and Indian-Owned Economic Enterprises—DOD Contracts] in [PBSCs] that either are not commercial items, or are treated as commercial items solely as a result of the authority in [section] 212.102."[15] The final rule applies to qualifying contracts or task orders entered into by or before 30 October 2003.[16]

Actual Use of PBSCs Occurring, but More Guidance Is Needed

In a recent report, the GAO concluded that while agencies are using PBSCs, agencies need more guidance to increase their understanding of PBSCs and the best ways take advantage of the methodology.[17] The GAO evaluated twenty-five service contracts that various agencies, including the DOD, characterized as performance-based, to determine whether the contracts indeed contained performance-based attributes.[18] Of the contracts the GAO examined, nine "clearly exhibited" the identified performance-based attributes.[19] Most of these contracts were for rather uncomplicated services, such as custodial services and building maintenance. The GAO also found four contracts for similar services that "could have incorporated all of the attributes but did not."[20] The twelve remaining contracts involved more complex and technical services, which were unique to the government or high risk in nature.

Because of the risk and complexity of these contracts, the GAO found that while the agencies incorporated some performance-based attributes, the contracts also included detailed specifications or other measures to ensure oversight control.[21] Citing "concern" as to whether agencies had a good understanding of performance-based contracting or knew how to best take advantage of the methodology, the GAO concluded that more and better guidance is necessary, especially "when acquiring more unique and complex services that require strong government oversight."[22] The GAO also learned that agency officials needed better criteria for determining which contracts should in fact be labeled "performance-based."[23] Major Huyser.

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14. *Id*.

15. *Id*.

16. *Id*.

17. GEN. ACCT. OFF., REP. NO. GAO-02-1049, *Contract Management: Guidance Needed for Using Performance-Based Service Contracting* (Sept. 2002) [hereinafter GAO-02-1049]. "In 2001, agencies reported using performance-based contracting methods on about $28.6 billion, or twenty-one percent of the $135.8 billion total obligations incurred for services." *Id*. at 3.

18. Based on guidance from the Office of Federal Procurement Policy (OFPP), the GAO evaluated the purported PBSCs for the following attributes:

> 1. Describe the requirements in terms of results required rather than the methods of performance of the work;
> 2. Set measureable performance standards;
> 3. Describe how the contractor's performance will be evaluated in a quality assurance plan;
> 4. Identify positive and negative incentives, when appropriate.

Id. at 3-4; *see also* FAR, *supra* note 6, at 37.601.

19. GAO-02-1049, *supra* note 17, at 4.

20. *Id*. at 6. For example, a Treasury Department contract for dormitory management contained forty-seven pages of specifications that detailed such requirements as the cotton-polyester fiber content of towels, the components necessary for making beds, and the minimum thickness standards for trash can liners. *Id*.

21. *Id*. at 7. For example, the operation of a nuclear facility and Navy tactical test ranges. *Id*.

22. *Id*. at 8. In response to the GAO's report, the OFPP indicated that it was "in the initial stages of developing new guidance examining how to improve agencies' use of performance-based contracting." *Id*. Acquisition officials seeking assistance on procuring and managing PBSCs in the interim may wish to consult a new interagency Web-based guide entitled *Seven Steps to Performance-Based Services*. This guide, developed by the Department of Commerce in coordination with other agencies, such as the DOD and the General Services Administration, is available at http://oamweb.osec.doc/pbsc/index.html.

23. *Id*. at 8.

Procurement Fraud

Supremes to Decide Whether Municipalities Are People Too

In one of the more important developments this year, the U.S. Supreme Court granted certiorari in a case involving the status of municipalities under the False Claims Act (FCA).[1] On 28 June 2002, the Justices issued a writ of certiorari to the Court of Appeals for the Seventh Circuit, deciding to hear the case of *United States ex rel. Janet Chandler v. Cook County* (*Chandler*).[2]

The grant of certiorari follows a 2000 Supreme Court decision involving the status of states under the FCA. In *Vermont Department of Natural Resources v. United States ex rel. Stevens* (*Stevens*),[3] the Court decided that states are not "persons" for False Claims Act (FCA) purposes. The Court partially based its decision on the longstanding interpretive presumption that a "person" does not include the "sovereign" (for example, a sovereign state). The Court held that it could only disregard this presumption of sovereignty if it saw some affirmative showing of statutory intent to the contrary. The Court could not find any affirmative indications that the term "person" included states for purposes of *qui tam* liability in either the FCA's text or its legislative history.[4] The conclusion was further buttressed by the rule of statutory construction that if Congress intends to alter the usual constitutional balance between states and the federal government, it must make its intention to do so unmistakably clear in the statute's language.[5] The *Stevens* decision left open the question of whether non-state units of local government could be "persons" for purposes of the FCA.

In *Chandler*, Doctor Janet Chandler brought a *qui tam* action against Cook County, Illinois, alleging misconduct in the handling of a $5 million federal research grant that the federal government gave Cook County Hospital to study the treatment of drug-dependent pregnant women. The allegations of misconduct included treating "ghost" participants who did not exist and tampering with test protocols. At the district court, Cook County filed a motion to dismiss the FCA action on the grounds that it was not a "person" for purposes of the FCA.[6] Cook County relied heavily on the Supreme Court's *Stevens* decision, arguing that the same logic applied to municipal governments. The county further argued that the FCA's treble damages were punitive, and thus violated the long-standing common law rule against assessing punitive damages against municipal units of government.[7]

The judge denied the county's motion. Specifically, the court concluded that the *Stevens* reasoning did not apply to municipalities and other non-state units of local government.[8] One provision that swayed the Court was the Civil Investigative Demand of the FCA, which defined "person" as "any natural person, partnership, corporation, association, or other legal entity, including any State or political subdivision of a State."[9] The district court further held that the FCA treble damages provision was not punitive; thus, this provision did not violate, impinge on, or implicate municipalities' traditional immunity from punitive damages.[10]

On appeal, the U.S. Court of Appeals for the Seventh Circuit painstakingly analyzed the Supreme Court's *Stevens* decision and concluded that its reasoning did not protect municipalities from liability under the FCA. Specifically, the Seventh Circuit found that the presumption that a "person" does not include a state protects the standing of states as sovereign units of government under the American system of federalism. The court concluded that the presumption "cuts the other way for municipalities" because "the Supreme Court has never imposed the

1. 31 U.S.C. §§ 3729-33 (2000). The FCA is the primary civil remedy for combating procurement fraud. It imposes liability on any "person" who "knowingly presents or causes to be presented," a false or fraudulent claim, or conspires to defraud the government by having a false or fraudulent claim allowed or paid. The act allows for treble damages, in addition to civil penalties in the amount of $5000 to $10,000 per claim. The FCA also allows an individual to bring suit in the name of the United States under the *qui tam* provisions of the FCA. *Id.*

2. 277 F.3d 969 (7th Cir.), *cert. granted*, 122 S. Ct. 2657 (2002).

3. 529 U.S. 765 (2000).

4. *Id.* at 787-88.

5. *Id.* at 786-88.

6. Chandler v. Hektoen Inst., 35 F. Supp. 2d 1078 (N.D. Ill. 1999).

7. *Chandler*, 277 F.3d at 977 (discussing City of Newport v. Fact Concerts, 453 U.S. 247 (1981)).

8. *Id.* at 972-73 (discussing *Chandler*, 35 F. Supp. 2d at 1084).

9. *See* 31 U.S.C. § 3733(l)(4) (2000); *Chandler*, 35 F. Supp. 2d at 1084.

10. *Chandler*, 35 F. Supp. 2d at 1084. Shortly after the Supreme Court decided *Stevens*, Cook County filed a motion requesting that the district court reconsider its decision. In light of the *Stevens* decision, the district court held that the treble damages provision of the FCA was punitive and dismissed the case against Cook County. Doctor Chandler subsequently appealed the second decision to the Court of Appeals. *See Chandler*, 277 F.3d at 970; Chandler v. Hektoen Inst., 118 F. Supp. 2d 902 (2000).

same requirement on Congressional efforts to make municipal entities amenable to federal legislation."[11]

The Fifth Circuit has also examined the issue of municipal immunity under the FCA, and in an equally well-reasoned opinion, held that municipalities are not "persons" for purposes of the FCA, and are thus shielded from liability under the Act.[12] Specifically, the Fifth Circuit held that the treble damages provision of the FCA is punitive and thus violates the common-law rule that municipalities are immune from punitive damages in civil proceedings.[13] Who is right and who is wrong in the eyes of the Supreme Court? Stay tuned.

How Original Is Original?

Although the pending *Chandler* case seems to be taking up most of the *qui tam* limelight this year, no *Year in Review* would be complete without at least passing mention of one "original source" case. In *United States ex rel. Minnesota Association of Nurse Anesthetists v. Allina Health Systems Corp.*,[14] the U.S. Court of Appeals for the Eighth Circuit examined the "original source" requirement under the FCA[15] and joined the majority of federal appellate courts, holding that the FCA prohibits claims that are "supported by" facts that were "publicly disclosed" before a relator brings a *qui tam* action.[16] In adopting this standard, the court rejected the minority test, which interprets "based upon" a "public disclosure" to mean "derived from."[17] The court reasoned that the minority's interpretation of the "based upon" exception makes it virtually impossible for a would-be *qui tam* relator to bring an action. Specifically,

> [I]f a suit is only based upon a public disclosure if it results from the disclosure, as the minority interpretation would have it, then the statute's additional provision allowing suit if the relator is "an original source" of the underlying information is of no effect, because no one could be an original source if his knowledge was derived from public disclosure.[18]

The court reasoned that it is "inconceivable that Congress would have drafted the statute so poorly as to have included a provision that could never have any effect."[19]

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11. *Chandler*, 277 F.3d at 980-81.

12. United States *ex rel.* Garibaldi v. Orleans Parish School Bd., 244 F.3d 486 (5th Cir. 2001).

13. *Id*. at 491.

14. 276 F.3d 1032 (8th Cir. 2002).

15. The FCA provides,

> No court shall have jurisdiction over an action under this section based upon the public disclosure of allegations or transactions in a criminal, civil, or administrative hearing, in a congressional, administrative, or Government [General] Accounting Office report, hearing, audit, or investigation, or from the news media, unless the action is brought by the Attorney General or the person bringing the action is an original source of the information.

31 U.S.C. § 3730(e)(4) (2000). Subsection (B) of this statute defines "original source" as: "an individual who has direct and independent knowledge of the information on which the allegations are based and has voluntarily provided the information to the Government before filing an action under this section which is based on the information." *Id*. § (e)(4)(B).

16. The majority view is that a *qui tam* suit is "based upon" a public disclosure whenever the allegations in the suit and in the disclosure are the same, "regardless of where the relator obtained his information." *Minn. Ass'n of Nurse Anesthetists*, 276 F.3d at 1045; *see also* United States *ex rel.* Mistick PBT v. Housing Auth., 186 F.3d 376, 385-88 (3d Cir. 1999), *cert. denied*, 529 U.S. 1018 (2000); United States *ex rel.* Lamers v. City of Green Bay, 168 F.3d 1013, 1017 (7th Cir. 1999); United States *ex rel*. Biddle v. Bd. of Trustees of the Leland Stanford, Jr., Univ., 161 F.3d 533, 536-40 (9th Cir. 1998); United States *ex rel.* McKenzie v. Bell South Telecom., Inc., 123 F.3d 935, 940 (6th Cir. 1997); United States *ex rel.* Findley v. FPC-Boron Employees' Club, 105 F.3d 675, 682-85 (D.C. Cir. 1997); Cooper v. Blue Cross and Blue Shield, 19 F.3d 562, 567 (11th Cir. 1994); United States *ex rel*. Precision Co. v. Koch Indus., Inc., 971 F.2d 548, 552-53 (10th Cir. 1992); United States *ex rel.* Doe v. John Doe Corp., 960 F.2d 318, 324 (2d Cir. 1992).

17. *Minn. Ass'n of Nurse Anesthetists*, 276 F.3d at 1045. The minority view, which is shared by only the Fourth Circuit and one panel of the Seventh Circuit (in schism with another panel), is that "based upon" should be given its ordinary meaning of "derived from," so that the *qui tam* allegation must have resulted from the disclosure in order to bar jurisdiction. *Id.* at 1044-1045; *see* United States v. Bank of Farmington, 166 F.3d 853, 863 (7th Cir. 1999); United States *ex rel.* Siller v. Becton Dickinson & Co., 21 F.3d 1339, 1348 (4th Cir. 1994).

18. *Minn. Ass'n of Nurse Anesthetists*, 276 F.3d at 1045; *see also Eighth Circuit Adopts "Supported By" Reading of the FCA Public Disclosure Bar, but Finds Association Is "Original Source,"* 44 GOV'T CONTRACTOR 6, ¶ 60 (Feb. 13, 2002).

19. *Minn. Ass'n of Nurse Anesthetists*, 276 F.3d at 1045.

Greed Is Good (Not!)

On 3 July 2002, a federal grand jury indicted five individuals for their alleged involvement in a bribery scheme in Korea. Those indicted include Colonel (COL) James Moran, Commander of the U.S. Army Contracting Command, Korea (USA-CCK); COL Moran's wife, Gina Moran; and three other civilians allegedly involved in the bribery scheme. The scheme centered around COL Moran, who allegedly influenced the award of several contracts after soliciting bribes. As the commander of the USA-CCK, COL Moran oversaw an agency that awarded more than $300 million worth of contracts each year.[20] COL Moran recently agreed to plead guilty to soliciting more than $800,000 in bribes, and Mrs. Moran will plead guilty to making a false statement.[21]

The indictment alleged that COL Moran improperly influenced the award of at least four contracts. The contractors paid COL Moran primarily in $100 bills; in one instance, he demanded $500,000 for his services. Since the contractor did not have the total amount available, COL Moran put the contractor on an installment plan.[22]

During the search of COL Moran's quarters, Army Criminal Investigation Division (CID) agents seized approximately $700,000 in $100 bills. Gina Moran, who was indicted for obstruction of justice, allegedly attempted to move money from the living room sofa to the bedroom during the search.[23]

Enron, Arthur Andersen Suspended

On 15 March 2002, the General Services Administration (GSA) suspended Enron Corporation, Arthur Andersen, and several present and former Enron and Arthur Andersen officials from conducting new business with the federal government. The GSA's reason for the suspensions is "adequate evidence" that Enron and Andersen "engaged in misconduct and lacked internal controls."[24] The suspensions are for twelve months for all parties, except for Arthur Andersen, which was suspended for the duration of its indictment.[25]

Both Enron and Andersen did relatively little business with the government. In the latest list of top government contractors, Andersen hardly made it to the ranks of the top two hundred. Enron did not even make the list.[26] The government has not suspended WorldCom, whose former Chief Financial Officer has been indicted for fraud.[27] WorldCom is ranked as the twenty-sixth-largest contractor with the DOD, and the forty-sixth largest contractor government-wide.[28]

The suspensions of Enron and Arthur Andersen set an interesting precedent because the stated reason for the suspensions did not involve their performance on government contracts. In fact, the GSA has conceded that there have been no performance problems with either Enron or Arthur Andersen on any government contract. At least one commentator has noted that the suspensions introduce an unwarranted degree of political subjectivity into the suspension and debarment process.[29]

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20. Press Release, Office of the U.S. Attorney for the Central District of California (July 3, 2002) [hereinafter DOJ Press Release], *available at* http://www.usdoj.gov/usao/cac/pr2002/103.html. The indictment is available on FindLaw, at http://news.findlaw.com/hdocs/docs/crim/usmoran702ind.pdf.

21. Monte Morin, *Army Officer to Admit He Solicited Kickbacks*, L.A. TIMES, Jan. 25, 2003.

22. DOJ Press Release, *supra* note 20. The indictment alleged that COL Moran agreed to award a local contractor a contract for a barracks upgrade and renovation project in exchange for a $500,000 bribe. Mrs. Moran, who coordinated the transfer of money and information between COL Moran and various contractors, was able to collect $150,000 from the contractor on this contract before their arrest. COL Moran was also accused of taking bribes to fix the contract for the Korean security guards who protect the gates of several U.S. installations. *Id.*

23. *Id*.

24. *See* Kellie Lunney, *GSA Suspends Enron and Andersen from New Business*, GOV'T EXEC. MAG., March 15, 2002, *at* http://www.govexec.com/dailyfed/0302/031502m2.htm.

25. *Id*. On 15 June 2002, a federal jury convicted Arthur Andersen of obstruction of justice and for impeding a federal investigation into the financial collapse of Enron. Soon afterward, Andersen informed the government that it would cease auditing public companies, effectively ending the life of the eighty-nine-year-old firm. Kurt Eichenwald, *Arthur Andersen: Guilty as Charged*, N.Y. TIMES, June 16, 2002, *available at* www.nytimes.com/2002/06/16/business/yourmoney/16HANK.html.

26. *See Top 100 Defense Contractors*, GOV'T EXEC. MAG., Aug. 15, 2002, *available at* http://www.govexec.com/top200/02top/s3chart1.htm.

27. *See* Brock N. Meeks, *Ex-WorldCom CFO Indicted*, MSNBC.com, Aug. 28, 2001, *at* http://www.msnbc.com/news/800173.asp.

28. *See Top 100 Defense Contractors*, *supra* note 26. Specifically, WorldCom did $513,666,000 in business with the U.S. Government during fiscal year 2001. The vast majority of that business ($483,369,000) was with the DOD. *Id.*

29. *See* Steven L. Schooner, *Suspensions Are Just a Side Show*, GOV'T EXEC. COM., May 1, 2002, *at* http://www.govexec.com/features/0502/0502view1.htm.

Contractor Blacklisting Rule Scrapped

In a move of dubious timing, the Bush administration recently revoked a Clinton-era policy that set ethics, labor, and environmental standards for companies seeking to do business with the federal government.[30] The revocation took effect on 27 December 2001, just weeks before the Enron and Arthur Andersen debacles became front-page news.

Last year's *Year in Review* reported that on 20 December 2000, the Federal Acquisition Regulation (FAR)[31] Council published a "final rule" in the *Federal Register* addressing contractor responsibility, labor relations, and environmental standards.[32] The rule generated considerable controversy, and on 3 April 2001, under a new Administration, the FAR Council published a new rule staying enforcement of the final rule until it determines whether the burdens imposed by the rule outweighed its benefits.[33] During the period of the stay, the FAR Council recommended revoking the rule in its entirety. In the text of the Federal Register, the FAR Council noted that "contracting officers will continue to have the authority and duty to make responsibility decisions," and "debarring officials will continue to have the authority and duty to make determinations whether to suspend or debar a contractor."[34]

Hit the Road Jack, and Don't You Come Back
No More, No More, No More, No More . . . .

The General Accounting Office (GAO) is no longer in the suspension and debarment business. In *Shinwha Electronics*,[35] Shinwha protested the Army's decision to suspend it from competing on future government contracts pending completion of a criminal investigation. When the Army issued the suspension, Shinwha was under investigation for allegedly submitting falsified payment records for work it did not actually perform on a contract for the maintenance and repair of fire safety systems at American military installations in Korea. The suspension precluded Shinwha from competing on a contract for the maintenance and repair of a fire alarm and detection system at Kunsan Air Base, Korea.[36] Because the suspension came on the heels of another procurement in which it was competing, Shinwha asserted that it had standing to bring the protest before the GAO as an "interested party."[37] Shinwha also demanded to see all the evidence upon which the government based the suspension, and noted in passing that the government had obtained much of its information in violation of the attorney-client privilege.[38]

The GAO agreed to hear the protest because the suspension occurred on the heels of the fire alarm contract. Beyond that, the GAO was unimpressed with Shinwha's case. The GAO examined the Army's procedures and concluded that the Army acted reasonably in protecting its rights under the FAR to suspend a contractor from the award of future contracts where the Army suspected misconduct. The GAO also observed that under the FAR, Shinwha had no right to see the government's case during an ongoing criminal investigation. Simply put, "the protestor was afforded the level of due process to which it [was] entitled."[39] More important than the plight of Shinwha is the revelation that the GAO will no longer review cases involving suspension and debarment. The GAO noted that the FAR sets forth specific procedures for both imposing and challenging a suspension or debarment action.[40]

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30. 66 C.F.R. pt. 248 (2002); *see also* Jason Peckenpaugh, *Bush Administration Scraps Contractor Responsibility Rule*, GOV'T EXEC. COM., Dec. 28, 2001, *at* http://www.govexec.com/dailyfed/1201/122801pl.htm.

31. GENERAL SERVS. ADMIN. ET AL., FEDERAL ACQUISITION REG. (July 2002) [hereinafter FAR].

32. 65 C.F.R. pt. 80,255 (2000); *see also* Major John J. Siemietkowski et al., *Contract and Fiscal Law Developments of 2001—The Year in Review,* ARMY LAW., Jan./Feb. 2002, at 55 [hereinafter *2001 Year in Review*].

33. 66 C.F.R. pt. 17,754.

34. 66 C.F.R. pt. 248 (2002). In an interesting development, on 26 September 2002, the *Government Executive* leaked word that the Office of Government Ethics issued a letter to attorneys and ethics officials, requesting feedback as to whether there should be a mandatory "code of conduct" for companies that do business with the government. *See* Shane Harris, *Ethics Office Launches Inquiry into Procurement Practices*, GOV'T EXEC. COM., Sept. 26, 2002, *at* http://www.govexec.com/dailyfed/0902/0902602h1.htm. The GAO also recently revised the "independence standard" set forth in *Government Auditing Standards*, otherwise known as the *Yellow Book*. This is part of a complete overhaul of the *Yellow Book*, spurred on in part by the Enron and Arthur Andersen debacles. *Id.*; *see supra* Part IV T (discussing the "independence standard" in relation to the *Government Auditing Standards*).

35. Shinwha Elecs., B-290603, B-290603.2, 2002 U.S. Comp. Gen. LEXIS 130 (Sept. 3, 2002).

36. *Id.* at *2.

37. *Id.* at *1.

38. *Id.*

39. *Id.* at *5.

A Raisin in the Sun

In a case that has many in the government procurement community upset, the Court of Federal Claims (COFC) recently held that the U.S. Department of Agriculture (USDA) acted arbitrarily and capriciously in suspending a raisin contractor after awarding five previous contracts to the contractor, and when the USDA was aware of the misconduct at the time it awarded the previous contracts. In *Lion Raisins*,[41] the USDA suspended Lion from contracting with the government for one year. The suspension was based on a USDA investigation that revealed that Lion had forged several raisin certifications, and on at least one certification, changed the certificate for the grade of raisins from "Grade C" to "Grade B."[42] The USDA completed the preliminary report of investigation on 26 May 1999, but did not issue the notice of the suspension until 12 January 2001.[43] From the date the USDA completed its preliminary report until it issued the suspension notice, Lion and the USDA entered into five relatively small contracts for the sale of raisins. After the USDA issued the suspension notice, Lion was precluded from bidding on a much larger contract.[44]

Shortly after the USDA issued the suspension notice, Lion requested a hearing. During the hearing, Lion's vice president, Mr. Bruce Lion, noted that the misconduct was the result of a rogue employee who had since been fired and subsequently convicted for stealing company funds. Mr. Lion also identified fraud abatement measures he took to ensure that the problems would not be repeated (such as, video surveillance, better inspection processes, etc.), and requested that the suspension be lifted. The USDA was unimpressed and issued a final decision upholding the suspension.[45] At the COFC, Lion filed a motion for summary judgment to overturn the USDA's suspension. Lion also asked for bid preparation costs and lost profits for the contract on which Lion was precluded from bidding.[46]

The COFC concluded that the USDA acted in an arbitrary and capricious manner in suspending Lion. Specifically, the court admonished the USDA for awarding five contracts to Lion between the date the USDA completed the preliminary investigation and the date it issued the suspension notice. The COFC emphasized that the USDA made five affirmative responsibility determinations before it issued the five contracts. Based on the same available evidence, however, the suspending authority found Lion to not be a responsible contractor.[47] In granting Lion's motion for summary judgment, the court reversed the USDA decision to suspend Lion, but denied Lion's request for lost profits.[48]

From the government's standpoint, *Lion Raisins* is problematic for several reasons. Practically, it is often imprudent to suspend a contractor who is the subject of an investigation prematurely; the early disclosure of evidence may hinder other aspects of the case, such as criminal prosecution. In this case, the court explicitly stated that it was not holding that it was *per se* arbitrary and capricious for the government not to suspend a contractor immediately pending further investigation.[49] The decision, however, clearly undercuts the government's ability to time a suspension so that it does not jeopardize an ongoing investigation. Arguably, the decision may foster a "use it or lose it" attitude in cases of suspected procurement fraud (that is, the government will waive the right if it does not exercise it quickly). The decision is also problematic in that it grants a quasi-res judicata status to contracting officers' responsibility determinations in later suspension and debarment proceedings. Quite simply, it is inconceivable that a contracting officer's potentially erroneous determination of affirmative responsibil-

40. *Id.* at *6; *see also* FAR, *supra* note 31, §§ 9.406-3(b), 9.407-3(b). Although the GAO will no longer entertain protests involving suspensions and debarments, contractors are not without options beyond the agency level. Pursuant to the Tucker Act, the Court of Federal Claims (COFC) has jurisdiction to review post-award bid protests, including those predicated on agency suspension or debarment actions, where the protestors can establish "irreparable injury." *See* 28 U.S.C. § 1491(b) (2000). Typically, the COFC will find irreparable injury when the government announces an invitation for bids or proposals, and but for the suspension or the debarment, the suspended or disbarred contractor could have competed for the contract. The court must set aside agency decisions that are "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law" or made "without observance of procedure as required by law." 5 U.S.C. § 706(2)(A), (D) (2000); *see also* Ramcor Serv. Group, Inc. v. United States, 185 F.3d 1286 (Fed. Cir. 1999) (explaining the adoption of agency review standards into Tucker Act amendments). Under the "arbitrary and capricious" standard, the court may not substitute its judgment for that of agency officials. Rather, inquiry must focus on whether the agency "examined the relevant data and articulated a satisfactory explanation for its action." Motor Vehicle Mfrs. Ass'n v. State Farm Ins., 463 U.S. 29, 43 (1983).

41. Lion Raisins v. United States, 51 Fed. Cl. 238 (2001).

42. *Id.* at 240.

43. *Id.* at 240-41.

44. *Id.* at 241-43.

45. *Id.* at 242.

46. *Id.* at 242-43.

47. *Id.* at 247-48.

48. *Id.* at 251; *see supra* Part II.O (discussing the court's decisions concerning lost profits under an implied-in-fact contract theory).

49. *Lion Raisins*, 51 Fed. Cl. at 249.

ity on a previous contract should bind suspension and debarment officials.

Busted: CAFC Upholds Use of CDA Anti-Fraud Provision

The government rarely uses the Contract Disputes Act's (CDA) Anti-Fraud provision.[50] As such, it is pure poetry to read a CAFC opinion that upholds the COFC when it allows the government to use the CDA's Anti-Fraud provision against a crooked contractor.[51]

In *Larry D. Barnes, Inc. v. United States*,[52] the government awarded Larry D. Barnes, also known as Tri-Ad Construction (Tri-Ad), a contract that required Tri-Ad, among other requirements, to perform excavation work in an area containing a large number of underground utility obstructions. During contract performance, Tri-Ad told the contracting officer that the number of underground obstructions Tri-Ad encountered greatly exceeded the number expected. Shortly thereafter, Tri-Ad issued a certified claim to the contracting officer for about $1.3 million, seeking compensation for differing site conditions, lost profits, a work stoppage, and "added costs" for which it offered no reasonable explanation. The contracting officer ordered an audit; the Defense Contract Audit Agency (DCAA) found the claim to be completely without merit and requested additional documents from Tri-Ad. Tri-Ad complied and offered additional explanations why it was entitled to additional money. Tri-Ad then amended its claim and reduced the requested amount to $808,000. The contracting officer then denied the amended claim, and Tri-Ad appealed the contracting officer's decision to the COFC.[53]

Tri-Ad fared poorly at trial. The government argued that Tri-Ad had violated three statutes: (1) the Forfeiture of False Claims Act;[54] (2) the Contract Disputes Act's Anti-Fraud Provision;[55] and (3) the False Claims Act.[56] The COFC agreed that Tri-Ad had violated all three statutes. On appeal to the CAFC, Tri-Ad disputed each statute's applicability, and once again fared poorly. Concerning the Forfeiture of False Claims Act, the CAFC observed that Tri-Ad's vice president testified that he knew that lost profits on deleted work were not recoverable, but "let it ride."[57] The court also observed that the weight of evidence, including Tri-Ad's own internal records, contradicted Tri-Ad's claims.[58] Concerning the False Claims Act violation, the court again concluded that the government had proved that Tri-Ad presented a false or fraudulent claim, or at the very best,

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50. 41 U.S.C. § 604 (2000); s*ee* United States *ex rel.* Wilson v. North Am. Constr., 101 F. Supp. 2d 500, 533 (S.D. Tex. 2000) (refusing to enforce 41 U.S.C. § 604, in part because there were "very few cases applying 41 U.S.C. 604").

51. *See* Larry D. Barnes, Inc. v. United States, No. 98-668C, slip op. (Ct. Fed. Cl. Aug. 31, 2000).

52. Larry D. Barnes, Inc. v. United States, No. 01-5020, 2002 U.S. App. LEXIS 16595 (Aug. 14, 2002).

53. *Id.* at *14-15.

54. 28 U.S.C. § 2514 (2000). The Forfeiture of False Claims Act provides:

> A claim against the United States shall be forfeited to the United States by any person who corruptly practices or attempts to practice any fraud against the United States in the proof, statement, establishment, or allowance thereof. In such cases the United States Court of Federal Claims shall specifically find such fraud or attempt and render judgment of forfeiture.

Id.

55. 41 U.S.C. § 604 (2000). The CDA Anti-Fraud provision states:

> If a contractor is unable to support any part of his claim and it is determined that such inability is attributable to misrepresentation of fact or fraud on the part of the contractor, he shall be liable to the Government for an amount equal to such unsupported part of the claim in addition to all costs to the Government attributable to the cost of reviewing said part of his claim. Liability under this subsection shall be determined within six years of the commission of such misrepresentation of fact or fraud.

Id.

56. 31 U.S.C. § 3729 (2000). The relevant section provides:

> (a) Liability for certain acts—Any person who—(1) knowingly presents, or causes to be presented, to an officer or employee of the United States Government . . . a false or fraudulent claim for payment . . . is liable to the United States Government for a civil penalty of not less than $5000 and not more than $ 10,000, plus [three] times the amount of damages which the Government sustains because of the act of that person . . . ."

Id.

57. *Larry D. Barnes*, 2002 U.S. App. LEXIS 16595, at *14.

58. *Id.* at *14-15.

acted with deliberate ignorance or reckless disregard of the claim's truth or falsity.[59]

This was not the first time the CAFC decided a case involving the CDA's Anti-Fraud Provision.[60] Nevertheless, given the lack of cases involving this provision, it is surprising that the court was very matter-of-fact in its analysis of the applicability of this provision. The court observed that Tri-Ad, in its certified claim, asserted that the government owed it over $1.3 million in nonexistent "added costs" due to, among other things, "loss of production."[61] To support this claim, Tri-Ad asserted various inconsistent explanations, all of which were rejected by the COFC.[62] Given that Tri-Ad deliberately pressed a fraudulent claim before the contracting officer and the COFC, the CAFC was more than willing to apply the CDA Anti-Fraud provision in this case.[63]

What Were You Thinking?—CAFC Reverses ASBCA in Fraud Case

Another CAFC case that will delight government procurement attorneys is *Navy v. Systems Management American Corp.*[64] In *Systems Management American* (*SMA*), it is not just the crooked contractor that fared poorly before the CAFC; the CAFC reversed the Armed Services Board of Contract Appeals (ASBCA) for its questionable decision to grant SMA's appeal in the face of obvious fraud. Specifically, in *SMA*, the CAFC reversed an ASBCA decision that awarded a contractor an equitable adjustment and breach damages when the agency denied the contractor the opportunity to bid on a contract because the contractor was under investigation for fraud involving a related contract.[65]

The Navy awarded SMA three contracts to procure "SNAP II," a computer system for various Navy surface ships and submarines. A necessary condition of the contract award was SMA's status as a small business under the Small Business Act.[66] In April 1987, SMA entered into a fourth contract with the Navy, which the parties initiated as a letter contract for a basic quantity of computer upgrades. The parties made this letter agreement subject to "definitization" by 30 September 1987, meaning that they had to set the price for both the base and option year equipment by that date.[67] In September 1987, SMA learned that under a policy established by the Small Business Administration (SBA), the contract had to be definitized by 21 October 1987. This was because SMA was "graduating" from the SBA program on that date, and under the SBA policy, SMA could no longer compete on contracts set aside for small businesses after that date.[68]

On 30 September 1987, the Navy and SMA agreed on a price for the base-year contract and entered into a modification establishing the contract price. In early October 1987, the parties agreed to a price on the option year. Because the option price exceeded the contracting officer's authority, the parties needed the approval of the Assistant Secretary of the Navy (Logistics and Shipbuilding) for the option. On 16 October 1987, however, a U.S. Attorney issued a press release stating that a former SMA employee had plead guilty to federal charges of conspiracy to defraud the government in a kickback scheme involving senior officials of SMA and purchase orders charged to a contract with the Navy. Because the investigation was still ongoing, the Assistant Secretary of the Navy delayed approval of the option, citing the "current [criminal] investigations regarding SMA."[69] Because of this delay, the SBA deadline of 21 October passed, rendering SMA ineligible for award of the contract option.[70]

As events unfolded, it became apparent that the concerns of the Assistant Secretary were warranted. In July 1991, SMA plead guilty to one count of conspiring to defraud the Navy for

59. *Id.* at *13-16.

60. *See* UMC Elecs. v. United States, 249 F.3d 1337 (Fed. Cir. 2001).

61. *Larry D. Barnes*, 2002 U.S. App. LEXIS 16595, at *18.

62. *Id.* at *18-19.

63. *Id.* at *16-19.

64. England v. Sys. Mgmt. Am. Corp., 38 Fed. Appx. 567 (Fed. Cir. 2002).

65. *Id*. at 567-68.

66. *See* 15 U.S.C. §§ 631(a), (d), (j), 697(c) (2000) (codifying Congress's policy of encouraging small businesses through assistance from the Small Business Administration).

67. *SMA*, 38 Fed. Appx. at 568.

68. *Id.* at 568-69.

69. *Id.* at 568.

70. *Id.*

actions relating to the first two contracts. Five SMA employees, including two senior vice presidents, also plead guilty to multiple counts of fraud related to the two contracts.[71] SMA eventually completed performance of the base-year requirements of the fourth contract, and in 1991 and 1994, filed claims with the contracting officer for an equitable adjustment.[72] SMA also claimed breach damages, arguing that the Navy failed to approve the options in a timely manner, as required under the letter contract. The contracting officer denied the claims, and SMA appealed to the ASBCA.[73]

In a split decision,[74] the board upheld the denial of the equitable adjustment claim, but partially sustained SMA's appeal of the breach claim.[75] Specifically, the board found that while the Navy had no obligation to exercise the options with SMA, the Secretary of the Navy acted in bad faith when he delayed the approval of otherwise finalized options. In sum, the board concluded that the Navy breached its duty to negotiate in good faith and awarded SMA $31,025 for preparation costs and interest.[76]

Two of the board's five judges dissented.[77] While they agreed with the majority that the parties had an agreement to negotiate in good faith, the issue then became whether the Navy Secretary acted arbitrarily and capriciously or otherwise acted in bad faith by delaying the approval of the options. In the dissenting judges' view, the Navy should not have to pay for SMA's failure to meet the SBA deadline.[78] As the dissent stated, "[SMA] and its employees engaged in criminal conduct under the very program now before us and must bear the natural and reasonable consequences that resulted from a revelation of such conduct."[79]

The Navy appealed the board's decision to the CAFC.[80] On appeal, the court agreed that the pertinent issue was whether the Navy, faced with credible evidence of fraud, acted in good faith in its dealings with SMA. The court agreed with the ASBCA's dissent.[81] The CAFC's reasoning was logical and to-the-point:

> [W]e believe the Board erred by concluding that the Assistant Secretary abused his considerable discretion and had "no reasonable basis" to support the decision to delay approval of SMA's definitized options. Simply put, we believe the Assistant Secretary could have reasonably deemed it in the best interests of his agency to secure additional information about a current criminal investigation involving SMA and the SNAP II program itself before approving these options. Indeed, we agree that had the Assistant Secretary acted otherwise, one might reasonably characterize his prompt approval of the parties' agreement as "derelict" or else unreasonable.[82]

The Sins of the Sub Shall Be Visited Upon the Prime—But Not This Time

The COFC recently thwarted the government in its efforts to use the FCA forfeiture provision at 28 U.S.C. § 2514[83] against a contractor whose subcontractor had criminally dumped PCBs and other pollutants into Baltimore Harbor. In *N.R. Acquisition Corp. v. United States*,[84] the Defense Reutilization and Marketing Service (DRMS) awarded Acquisition Corp. a contract

71. *Id.*

72. *Id*. at 568-69. At the hearing, SMA presented no evidence for its request for equitable adjustment. In the absence of any evidence to support the claim, the ASBCA treated the claims as abandoned and denied them. *See* Sys. Mgmt. Am. Corp., ASBCA Nos. 45704, 49607, 2000-2 BCA ¶ 31,112, at 153,662.

73. *SMA*, 38 Fed. Appx. at 569.

74. Anecdotally, split decisions from the ASBCA are rare.

75. SMA, 2000-2 BCA ¶ 31,112, at 153,662.

76. *SMA*, 38 Fed. Appx. at 569-70; *see also* SMA, 2000-2 BCA ¶ 31,112, at 153,663.

77. *SMA*, 38 Fed. Appx. at 570; *SMA*, 2000-2 BCA ¶ 31,112, at 153,664.

78. *SMA*, 38 Fed. Appx. at 570-71; *SMA*, 2000-2 BCA ¶ 31,112, at 153,664-65.

79. *SMA*, 38 Fed. Appx. at 570 (quoting *SMA*, 2000-2 BCA ¶ 31,112, at 153,665).

80. *Id.* at 568.

81. *Id.* at 571.

82. *Id.*

83. *See* 28 U.S.C. § 2514 (2000).

84. 52 Fed. Cl. 490 (2002).

under which Acquisition Corp. paid the DRMS $748,999 to scrap the recently decommissioned *USS Coral Sea.* Under the terms of the contract, the DRMS required Acquisition Corp. to perform the scrapping in accordance "with all applicable Federal, State, and Local laws, ordinances, regulations, etc., with respect to human safety and the environment."[85]

After contract award, Acquisition Corp. discovered the ship contained significantly higher levels of PCBs and asbestos than expected—so much so that Acquisition Corp. submitted a claim to the DRMS for $8,871,416 for clean-up and other related costs.[86] Acquisition Corp. subcontracted much of the work to Seawitch Salvage, which discovered a cost-effective way to reduce its cleaning-related expenses significantly—dumping the contaminated material into Baltimore Harbor. A court subsequently convicted Seawitch's owner and president, Kerry Ellis, for the illegal dumping. Acquisition Corp. continued to press the claim, however, and upon the DRMS's denial, appealed the matter to the COFC.[87]

At issue was whether Seawitch's criminal conduct served to forfeit Acquisition Corp's claim.[88] The government argued that the criminal actions of Seawitch should be imputed to the plaintiff, Acquisition Corp., because it had hired Seawitch, knowing that Seawitch was an unlicensed asbestos removal contractor, although the contract required the plaintiff to have licensed personnel perform the work.[89] In response, Acquisition Corp. argued that the court should deny the government's motion for summary judgment because Seawitch's violations of environmental law, standing alone, did not constitute "fraud" within the meaning of the FCA. Acquisition Corp. also argued that there were no grounds for imputing Seawitch's actions upon itself because it was not a party to Seawitch's conviction.[90]

The COFC concluded that it could not render judgment because too many questions remained unanswered. Specifically, the court observed that neither party had established the extent of Acquisition Corp.'s involvement in Seawitch's criminal misconduct.[91] The court thus denied both parties' motions and cross-motions pending resolution of the issue of Acquisition Corp.'s involvement, if any, in Seawitch's criminal conduct.[92]

High-Value Item Clause Does Not Negate Right of Government to Bring FCA Case

In a recent split decision by the U.S. Court of Appeals for the Sixth Circuit,[93] the court held that the FAR's High-Value Items Clause (HVIC)[94] did not preclude liability under the FCA.[95] In *United States ex rel. Roby v. Boeing*,[96] a relator brought a *qui tam* action against Boeing, alleging that Boeing and its supplier, Speco, had violated the FCA by making false statements about the manufacture and sale of defective transmission gears to the Army.[97] The government intervened in the action and alleged that the defective transmission gears were directly responsible for the crash of a Ch-47D Chinook helicopter over Saudi Arabia in January 1991. In response to the *qui tam* action, Boeing asserted, among other defenses, that the HVIC of the helicopter contract precluded liability under the FCA. Before trial, the

85. *Id.* at 491.

86. *Id.*

87. *Id.* at 492-93.

88. *Id.* at 495.

89. *Id.* at 495-96.

90. *Id.* at 496-97.

91. *Id.* at 501.

92. *Id.* at 501-02.

93. United States *ex rel.* Roby v. Boeing Co., 302 F.3d 637 (6th Cir. 2002).

94. The High-Value Item Clause at FAR section 52.246-24 provides:

> (a) Except as provided in paragraphs (b) through (e) of this clause, and notwithstanding any other provision of this contract, the Contractor shall not be liable for loss of or damage to property of the Government (including the supplies delivered under this contract) that—(1) Occurs after Government acceptance of the supplies delivered under this contract; and (2) Results from any defects or deficiencies in the supplies.

FAR *supra* note 33, at 52.246-24. The purpose of the clause is to reduce government procurement costs by limiting contractor risk. *See id.*

95. *See* 31 U.S.C. §§ 3729-33 (2000); *see also supra* note 1.

96. 302 F.3d 637 (6th Cir. 2002).

97. *Id.* at 639-40.

parties settled the claim. A $15 million portion of the settlement, however, was contingent upon the outcome of an interlocutory appeal to the Sixth Circuit. The issue on appeal was whether the HVIC precluded liability under the FCA.[98]

After the Court of Appeals examined the history and purpose of both the FCA and the HVIC, the majority concluded that the HVIC did not shield contractors from liability under the FCA.[99] Specifically, the majority concluded that Boeing's interpretation of the HVIC would preclude the government from ever recouping a civil penalty of more than $10,000 for damages sustained for a false claim involving a high-value item, even though the government's actual damages could be far greater.[100] The majority looked at Congress's explicit recognition while amending the FCA that a significant number of fraud cases involve high-dollar items. It struck the majority as "incongruous that the HVIC would relieve contractors for high-value items from the FCA's damages provision."[101]

Judge Boggs's dissent did not focus on the history of the FCA so much as the wording and history of the HVIC clause. Specifically, he noted that the original 1971 version of the DOD's self-insurance policy stated that the clause did not protect government contractors "when the defects or deficiencies in such supplies . . . resulted from fraud or gross negligence as amounts to fraud, on the part of *any personnel of the Contractor*."[102] He went on to observe that Congress changed the clause in 1974 at the behest of the defense industry. The reissued clause removed the phrase involving fraud and replaced it with language similar to the present clause, excluding only "willful misconduct or lack of good faith on the part of any of the Contractor's directors or officers, . . . managers, superintendents, or other equivalent representatives."[103] In light of the fact that Judge Boggs's analysis is not entirely unreasonable, regulators should consider revising the HVIC clause and re-inserting the fraud language. Major Dorn.

98. *Id.* at 640.

99. *Id.* at 649.

100. *Id.* at 641-42.

101. *Id.* at 645.

102. *Id.* at 651 (Boggs, J., dissenting).

103. *Id.* Because the misconduct involving the transmission gears did not involve the "contractor's directors, or officers, . . . managers, superintendents" or the like, both parties stipulated that the facts of the case did not implicate this specific provision. *Id.* at 641-42.

Taxation

Still Fretting Over the FRET

When the Department of Defense (DOD) purchases military tactical vehicles, it must pay Federal Retail Excise Tax (FRET) through the manufacturer.[1] The Internal Revenue Service (IRS) collects the tax and deposits it into the Highway Trust Fund to help maintain the nation's roads. The Secretary of the Treasury has the authority to exempt the federal government from certain excise taxes if he determines that imposing such taxes would create a substantial burden or expense.[2] In January 2002, the Secretary of Defense (SECDEF) requested that the Secretary of the Treasury exercise the exemption for the DOD. The SECDEF reasoned that the FRET imposes a "substantial and unreasonable expense" on the DOD, costing it $228 million over the next five years.[3] The SECDEF also noted that "[t]he military vehicles that pay FRET rarely use the highway systems that FRET supports."[4]

The Department of the Treasury (DOT) denied the DOD's request, citing a lack of evidence of substantial "nontax" burden or expense.[5] The letter also reiterates the DOT's longstanding policy of not exercising its exemption authority with respect to taxes dedicated to the Highway Trust Fund.[6]

Seeing Red over a Piece of Green Paper

The Court of Appeals for the Federal Circuit (CAFC) recently affirmed a decision from the Court of Federal Claims (COFC) denying a contractor's claim for reimbursement for sales and use taxes, which the contractor failed to include in its fixed-price bid.[7] The contractor argued that the government had a duty to clarify an ambiguity in the solicitation, an ambiguity which was created by the inclusion of a "Special Tax Notice" printed on green paper.[8]

The CAFC held that the Special Tax Notice did not introduce ambiguity because it did not contradict the plain language of the Federal Acquisition Regulations (FAR).[9] The CAFC also concluded that the Special Tax Notice did not obligate the government to designate the contractor as its agent to qualify for an exemption under state law.[10]

Hercules Had a Weak Argument

In *Hercules Inc. v. United States*,[11] the CAFC affirmed the COFC's conclusion that the incorporated FAR "Taxes,"[12] "Credits,"[13] and "Allowable Cost and Payment"[14] provisions do not conflict with Cost Accounting Standard (CAS) 406 because CAS 406 does not require the allocation of tax refunds as independent indirect costs. Hercules contended that CAS 406 requires the government to follow the traditional cost accounting practice of including state income tax refunds in its mea-

1. The excise tax on the retail sale of heavy trucks and trailers is twelve percent. 26 U.S.C. §§ 4051-4053 (2000).

2. *Id*. § 4293.

3. Letter from the Honorable Donald H. Rumsfeld, Secretary of Defense, to the Honorable Paul H. O'Neill, Secretary of Treasury (29 Jan. 2002) (on file with author).

4. *Id*.

5. Letter from Mark A. Weinberger, Assistant Secretary of Treasury (Tax Policy), to the Honorable Donald H. Rumsfeld, Secretary of Defense (11 Apr. 2002) (emphasis added) (on file with author). The DOT's view is that the amount of the tax is not the type of burden to which the exemption should apply because the net revenue effect of a tax on the government is always zero. The DOT's letter cites legislative history to support its position that the burden or expense relates to "paperwork, inconvenience, and simplicity rather than the amount of the tax." *Id.*

6. *Id*. (citing the denial of past DOD exemption requests in 1984 and 1999, a 1996 Department of Energy request, and a 1991 Forest Service request).

7. Hunt Constr. Group, Inc. v. United States, 281 F.3d 1369 (2002).

8. *Id*. at 1372. The "green sheet" advised bidders that sales and use tax exemptions should be sought where applicable. *Id.*

9. *Id*. (citing General Servs. Admin. et al., Federal Acquisition Reg. 52.229-3 (July 2002) [hereinafter FAR]). Under this section of the FAR, the contract price includes all applicable federal, state, and local taxes and duties. *Id.*

10. *Hunt Constr.*, 281 F.3d at 1372. The CAFC was aware that the government disfavors agency agreements, citing a FAR section which provides that: "Prime contractors and subcontractors shall not normally be designated as agents of the Government for the purpose of claiming immunity from State or local sales and use taxes." FAR, *supra* note 9, at 29.303(a).

11. 292 F.3d 1378 (2002).

12. FAR, *supra* note 9, at 31.205-41(d).

13. *Id*. at 31.201-5.

14. *Id*. at 52.216-7(h)(2).

surement of tax costs in the year it receives the refunds.[15] Instead, the CAFC agreed with the government's interpretation that incorporated FAR clauses clearly state that any refund of a tax allowed as a contract cost must be credited or paid to the government using the same factors as when costs were originally deemed reimbursable.[16]

Don't Buck the Result, However Derived

In *Western Kentucky Coca-Cola Bottling Co. v. Revenue Cabinet*,[17] the Kentucky Court of Appeals held that the sale of canned soft drinks to the Army-Air Force Exchange Service (AAFES) for resale in vending machines was immune from the imposition of state sales tax under the Buck Act.[18] While its opinion contained a lengthy discussion of case law governing federal sovereign immunity,[19] the court relied most heavily on Section 107 of the Buck Act to arrive at its conclusion that the sales to AAFES were immune from sales tax.[20]

Although the court reached the same conclusion as the Kentucky Board of Tax Appeals (KYBTA), it did not invoke an exemption contained in the applicable Kentucky tax regulations.[21] The KYBTA did invoke the exception, which precluded the application of sales tax to receipts from sales to instrumentalities of the federal government. The *Western Kentucky* court did not explain why it did not rely on Kentucky's tax regulation.[22]

National Park Service Tells County Where to Park It

An Edmonson County, Kentucky, ordinance imposes a license tax on recreational businesses and businesses providing ticketing or reservation services for recreational businesses.[23] The tax was the lesser of twenty percent of the cost of each ticket or fifty cents per ticket. The Department of Interior, through its National Park Service (NPS), uses a contractor, Biospherics, Inc., to operate a nationwide computerized reservation and ticketing system for admission to national parks, including Mammoth Cave National Park in Edmonson County, Kentucky. Biospherics operates from a facility in Cumberland, Maryland. The NPS pays Biospheric a flat rate for each sale. Biospherics then transfers all payments by the visitors for admission or tours to the United States. When Biospherics challenged the Kentucky tax, the Edmonson County Circuit Court upheld its validity. The federal government directed that Biospherics stop paying the tax and filed suit in the U.S. District Court for the Western District of Kentucky.[24] The court concluded that the recreational license tax violated both the Supremacy Clause[25] and the dormant Commerce Clause[26] of the Constitution.[27]

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15. *Hercules*, 292 F.3d at 1381.

16. *Id*. at 1382.

17. 80 S.W.3d 787 (Ky. App. 2001).

18. 4 U.S.C. §§ 105-110 (2000).

19. *Western Kentucky*, 80 S.W.3d at 791-93.

20. *Id.* Federal statute provides that the waivers of sovereign immunity under sections 105 and 106 "shall not be deemed to authorize the levy or collection of any tax on or from the United States or any instrumentality thereof." 4 U.S.C. § 107 (2000).

21. *See Western Kentucky*, 80 S.W.3d at 794-95. Kentucky law provides that the "sales tax does not apply to receipts from sales to the federal government." 30 KY. ADMIN. REGS. 235(1) (2000).

22. *See Western Kentucky*, 80 S.W.3d at 794-95.

23. EDMONSON COUNTY, KY. ORD. EC 98-20 (1998).

24. United States v. Edmonson County, No. 1:00CV-155-RG, 2001 U. S. Dist. LEXIS 17660 (D. Ky. Oct. 1, 2001).

25. The Supremacy Clause states:

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the *supreme Law* of the Land; and the Judges in every State shall be bond thereby, any Thing in the Constitution or laws of any State to the Contrary notwithstanding.

U.S. CONST. art. VI, cl. 2 (emphasis added).

26. "Dormant" refers to a negative command within the Commerce Clause, U.S. CONST. art. I, § 8, cl. 3, which gives Congress the power "[t]o regulate Commerce with foreign Nations, and among the several States." *Id.* The Supreme Court has held that the "dormant" Commerce Clause prohibits certain state taxation even when Congress has failed to legislate on the subject. *See, e.g.*, Oklahoma Tax Comm. v. Jefferson Lines, Inc., 514 U.S. 175, 179 (1995).

27. *Edmonson County*, 2001 U. S. Dist. LEXIS 17660, at *19.

The court held that the license tax violated the Supremacy Clause because it imposed a tax directly on the revenues and activities of the United States.[28] Further, the court found a violation of the dormant Commerce Clause because the tax was not applied to an activity with a substantial nexus to the county, was not fairly apportioned, and was not fairly related to services provided by the county.[29]

Statement About Mississippi Taxes Was Not Muddy

In *Holmes & Narver Constructors, Inc.*,[30] the Armed Services Board of Contract Appeals (ASBCA) denied a contractor relief on a claim that the government provided misleading tax information during the solicitation process. During a pre-proposal conference, the contracting officer deferred answering a question about the applicability of "Mississippi sales taxes" to the construction project, indicating that the Air Force would respond later in writing.[31] The subsequent amendment to the Request for Proposals (RFP) included a question and answer as follows:

> QUESTION: Are Mississippi State Taxes applicable?
> ANSWER: The State of Mississippi assesses a 3.5% contractor tax on all construction contracts over $10,000, except residential construction. However, it is the contractor's responsibility to ensure compliance with all state and local taxes.[32]

The contractor alleged that he relied on this information, and apparently without consulting with its own counsel, removed the cost of the sales tax from the proposal. Unfortunately, Mississippi has both a "sales tax" and a "contractor tax," and although the project was largely exempt from the contractor tax, it was still fully subject to the state's seven-percent sales tax. After the award, the contractor sought reformation of its contract to increase the price by the amount of the sales tax on a "mutual mistake" theory.[33] The contractor reasoned that the government's answer falsely implied that the project would be exempt from Mississippi sales tax.[34]

The ASBCA concluded that the Air Force did not misrepresent the applicability of Mississippi sales taxes to the project. The ASBCA observed that even though the government's response "was silent regarding sales tax," it "emphasized it was the 'contractor's responsibility to ensure compliance with all state and local taxes.'"[35] The ASBCA also pointed to the inclusion of the FAR's standardized taxes clause, which places the burden of determining which taxes apply to the contractor.[36]

House Has D.C.'s Number

In its most recent decision concerning 911 emergency surcharges, the General Accounting Office (GAO) examined whether the U.S. House of Representatives (House) must pay the 911 emergency surcharge and a right-of-way charge which appear on the House's monthly statement from its local telephone service carrier.[37] The GAO's analysis hinged on whether the emergency surcharges are taxes directly imposed on the federal government. If the surcharges were taxes, these "vendee taxes are not payable by the federal government unless expressly authorized by Congress."[38] The GAO concluded that the 911 emergency surcharge is a District of Columbia (DC) vendee tax which is specifically removed from the telephone company's base rate. The federal government is therefore immune from the 911 emergency surcharge.[39]

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28. *Id.*

29. *Id*. at *27-31.

30. ASBCA Nos. 52429, 52551, 02-1 BCA ¶ 31,849.

31. *Id*. at 157,395.

32. *Id*. at 157,395-96.

33. *Id*. at 157,396.

34. *Id.* "According to appellant, 'it did not occur to H&N that in response to the question whether Mississippi State Taxes were applicable, the Government would respond by mentioning only a type of tax that was not applicable, while failing to mention a different type of state tax that was applicable.'" *Id*.

35. *Id*. at 157,400.

36. *Id.* The FAR provides that provides that "the contract price includes all applicable Federal, State, and local taxes and duties." FAR, *supra* note 9, at 52.229-3.

37. 911 Emergency Surcharge and Right-of-Way Charge, Comp. Gen. B-288161, Apr. 8, 2002 (on file with author), *available at* http://www.gao.gov/decisions/appro/288161.htm.

38. *Id*. at 3.

39. *Id*. at 5.

The GAO reached a different conclusion regarding the right-of-way charge. Unlike the 911 emergency surcharge, the telephone company did not collect the right-of-way charge from its subscribers for the DC government's benefit. The GAO would have reached the same result even if the right-of-way charge was a "tax" instead of a "fee" because the legal incidence of that charge falls on the telephone company, not the end user.[40] The telephone company's ability to increase its rates to pass on the tax, and then to itemize it on the statement "does not necessarily mean that the legal incidence falls on the vendee."[41] The GAO concluded that the right-of-way charge is a rental fee, not a tax that falls on the federal government; the House may pay the charge.[42] Mrs. Patterson.

40. *Id*. at 6.

41. *Id*.

42. *Id*.

Contract Pricing

GAO Questions DOD's Use of TINA Waivers[1]

To determine whether proposed purchase prices are fair and reasonable, contracting officers can, under certain conditions, request certified cost or pricing data in accordance with the Truth in Negotiations Act (TINA).[2] The usual scenario for requiring certified cost or pricing data is sole-source contract actions that exceed $550,000.[3] The head of the contracting activity (HCA), however, can grant a waiver from requiring submission of cost or pricing data under Federal Acquisition Regulation (FAR) section 15.403-1(b)(4), if there is sufficient information available to determine price reasonableness.[4] The General Accounting Office (GAO), however, recently reported that "[t]here was a wide spectrum in the quality of the data and analysis being used" to determine price reasonableness when the HCA waived certified cost or pricing data.[5]

The GAO recently noted that Congress expressed concern "that regulations do not provide adequate guidance on when waivers should be used."[6] The GAO reviewed "[twenty] waivers valued at more than $5 million each in fiscal year 2000" totaling approximately $4.4 billion.[7] To determine price reasonableness for these contracting actions with cost or pricing data waivers, the GAO found that most contracting officers conducted a price analysis by reviewing the proposed price without a supporting cost breakdown.[8] Although some of the price analyses involved complex price analysis methods or a review of uncertified cost data,[9] the GAO concluded, "[the Department of Defense (DOD)] is at a greater risk of inflated pricing because it is waiving the requirement [for certified cost or pricing data]."[10] The GAO ultimately recommended amendments to the FAR to "(1) clarify situations in which an exceptional case waiver may be granted, (2) identify what type of data and analyses are recommended for arriving at a price when waivers are granted, and (3) identify what kinds of outside assistance should be obtained."[11]

The DOD generally agreed with the GAO's findings, but disagreed with the recommendation to incorporate the guidance in the FAR. Instead, the DOD plans to incorporate the GAO's guidance in its Contract Pricing Reference Guides. The GAO, however, still believed that incorporating the guidance into the FAR "would help clarify the regulation" and is appropriate because the FAR "is the definitive source for contract management."[12]

"I Think I'll Take a Mulligan"
The ASBCA Reverses Its Defective Pricing Entitlement Decision in Its Quantum Decision

In the original *Black River Limited Partnership*[13] entitlement decision, the Armed Services Board of Contract Appeals (ASBCA) found that the appellant, Black River, was entitled to the reinstatement of a withdrawn equitable adjustment under a tax adjustment clause.[14] The tax adjustment clause provided for an upward adjustment to Black River's monthly capacity charge for a high temperature water (HTW) facility at Fort Drum when certain tax law changes affected their after-tax rate of return on the investment.[15] The originally withdrawn equita-

1. GEN. ACCT. OFF., REP. NO. GAO-02-502, *Contract Management: DOD Needs Better Guidance on Granting Waivers for Certified Cost or Pricing Data* (Apr. 22, 2002) [hereinafter GAO-02-502].

2. 10 U.S.C. § 2306a (2000); 41 U.S.C. § 254b (2000).

3. *See* GENERAL SERVS. ADMIN. ET. AL., FEDERAL ACQUISITION REG. 15.403-4(a)(1), 15.403-1(b) (July 2002) [hereinafter FAR].

4. *Id*. at 15.403-1(b)(4).

5. GAO-02-502, *supra* note 1, at 2.

6. *Id*. at 1.

7. *Id*. at 2.

8. *Id*. at 7.

9. *Id*. at 8.

10. *Id*. at 14.

11. *Id*. at 14-15.

12. *Id*. at 15.

13. ASBCA Nos. 46790, 47020, 97-2 BCA ¶ 29,077.

14. *Id*. at 144,752.

15. *Id*. at 144,716.

ble adjustment had provided for a rate of 68.6%.[16] The ASBCA, however, also determined that "[the] data supplied by appellant in support of its tax adjustment request . . . was not current, complete and accurate, as required by TINA, and thereby entitled the Government to a price adjustment under the contract."[17]

Due to the findings of entitlement for the government and Black River, the ASBCA remanded the case to the parties for quantum negotiations.[18] As often happens, Black River and the government were unable to agree on an adjusted amount for the capacity charge; accordingly, Black River brought a subsequent quantum appeal to the ASBCA.[19] In preparation for the hearing, Black River introduced proposed trial exhibits and testimony that related to the adequacy of its cost or pricing data submitted for the modification related to the tax adjustment clause.[20] Before the quantum appeal hearing, the government filed a motion in limine to exclude evidence of the cost or pricing data's adequacy because the earlier entitlement decision had ruled on that issue. The presiding judge denied the motion, but permitted the government to renew the motion in its post-hearing brief.[21]

In its brief, the government argued that the doctrines of law of the case and res judicata prevented Black River from relitigating matters presented and decided in the prior entitlement hearing.[22] Unfortunately for the government, this argument did not persuade the board. Specifically, the board decided that its prior ruling in the entitlement decision was not binding and considered the evidence necessary for resolving a central quantum issue before the board.[23] The board described this responsibility by stating, "The fact that our findings and conclusions here differ in some respects from those in our earlier decision does not stand in the way of our obligation to resolve the quantum issue."[24]

The board also noted that "[u]nder the law of the case doctrine, the judicial tribunal retains discretion to reconsider or consider more fully a prior ruling."[25] The board then denied the government's renewed motion and reconsidered the original TINA entitlement decision because the additional evidence was directly probative to the quantum decision.[26] The board also noted that:

> the far more extensive record [from the quantum hearing] presents evidence which is substantially different than in our earlier proceedings and, as reflected in [the findings and merits of the decision], our initial decision was clearly erroneous resulting in a manifest injustice to appellant to warrant our application of the exception to the law of the case doctrine.[27]

In contrast to its original decision, the board ultimately found that "[t]he data submitted to the government by appellant in support of its tax adjustment request did not violate TINA."[28]

"Son, I Do Not Want to Know About What Is in That Package You Were Carrying out of the Liquor Store, but Let's Open up a Bottle of Jack Daniels on Your 21st Birthday Next Week"

In *Aerojet Solid Propulsion Co.*,[29] the U.S. Court of Appeals for the Federal Circuit (CAFC) upheld an ASBCA decision holding that the TINA[30] required the disclosure of its receipt of sealed vendor bids during contract price negotiations with the

16. *Id.* at 144,724.

17. Black River Ltd. P'ship., ASBCA No. 51754, 02-1 BCA ¶ 31,839 (summarizing the ASBCA's reasoning in its subsequent quantum decision).

18. *Black River Ltd. P'ship*, 97-2 BCA ¶ 29,077, at 144,752.

19. *Black River Ltd. P'ship*, 02-1 BCA ¶ 31,839, at 157,310.

20. *Id.* at 157,319, 157,324.

21. *Id.* at 157,324.

22. *Id.* (describing and defining the law of the case doctrine).

23. *Id.* at 157,324-25.

24. *Id.* at 157,324.

25. *Id.*

26. *Id.*

27. *Id.* at 157,325.

28. *Id.* at 157,327.

29. Aerojet Solid Propulsion Co. v. White, 291 F.3d 1328 (Fed. Cir. 2002).

Army.[31] Aerojet was the military's sole supplier of nitroplasticizer, an ingredient used in ordnance propellants and some explosives. During price negotiations, Aerojet had presented the government a cost of $1.98 per pound for nitroethane, the primary component of nitroplasticizer. The costs of nitroethane and other components were derived from "price in effect" quotes from Aerojet's suppliers, which are not binding, but merely represent the current price.[32]

During the later stages of price negotiations, Aerojet solicited and received sealed bids for nitroethane from two of its suppliers. In accordance with Aerojet's internal policy, these bids remained unopened until after the bid deadline, which was after the conclusion of Aerojet's price negotiations with the Army. The Army negotiators were never informed of this, however, and they were unaware of the sealed bids Aerojet held. When the agency opened the sealed bids, the suppliers had quoted the price of nitroethane at $1.45 and $1.47 per pound.[33] After a post-award Defense Contract Audit Agency audit, the Army determined that the nondisclosure constituted defective pricing data, and the Army sought a $483,813 reduction in the contract price.[34] Aerojet disagreed and appealed the case to the ASBCA. The board held for the Army because the board determined that the existence of the unopened bids was relevant cost or pricing data that Aerojet should have disclosed during negotiations.[35] On appeal to the CAFC, the court affirmed the board's decision and stated:

> With chemical prices fluctuating wildly, a reasonable buyer or seller would recognize that mere knowledge of the undisclosed sealed nitroethane bids might give one negotiator an advantage during contract price negotiations. Hence, the Board did not err in determining that Aerojet's duty to disclose cost or pricing data required disclosure of the existence of the sealed nitroethane bids and the opening date of such bids.[36]

The court also noted that Aerojet would have had expectations of the current potential pricing quoted by its suppliers in the sealed bids. Depending on Aerojet's expectation of higher or lower pricing, as quoted in the sealed bids, the court believed that Aerojet could have delayed or hastened its negotiations with the Army to achieve its best bargaining position.[37] The court affirmed the ASBCA's decision, concluding:

> In sum, receipt of the new sealed nitroethane bids clearly was information a prudent buyer or seller reasonably would expect to affect price negotiations significantly. Therefore, Aerojet had an obligation to disclose their receipt under the plain language of [the TINA].[38]

Major Kuhn.

30. 10 U.S.C. 2306a (2000). The Truth in Negotiations Act requires offerors, contractors, and subcontractors to submit certified cost or pricing data during price negotiations of statutorily specified contracting actions. *Id.*

31. *See* Aerojet Solid Propulsion Co., ASBCA Nos. 44568, 46057, 00-1 BCA ¶ 30,855.

32. *Aerojet Solid Propulsion*, 291 F.3d at 1329.

33. *Id*.

34. *Id*. at 1330.

35. *See Aerojet Solid Propulsion*, 00-1 BCA ¶ 30,855.

36. *Aerojet Solid Propulsion Co.*, 291 F.3d. at 1331.

37. *Id*.

38. *Id*. at 1332.

Auditing

GAO Revises Auditor Independence Standard

With accounting scandals dominating headlines, the General Accounting Office (GAO) has revised the independence standard set forth in its publication, *Government Auditing Standards*, also known as the *Yellow Book*.[1] The January 2002 revision is part of a complete and ongoing overhaul of the *Yellow Book*.[2] The change, although not prompted by the most recent scandals, certainly will address them. As the Comptroller General noted in releasing guidance concerning the standard, "recent private sector accounting and reporting scandals have served to re-enforce the critical importance of having tough but fair auditor independence standards to protect the public and [e]nsure the credibility of the auditing profession."[3]

The independence standard is one of several legally binding professional requirements at the core of the accounting profession. These requirements range from those dealing with auditors' professional qualifications to the quality of audit efforts and characteristics of audit reports.[4] The *Yellow Book* specifies the standards applicable to audits of government organizations and functions;[5] its formulation of the independence standard provides that "in all matters relating to the audit work, the audit organization and the individual auditor, whether government or public, should be free both in fact and appearance from personal, external, and organizational impairments to independence."[6]

Amendment 3 covers a range of auditor independence issues, including the three general classes of independence "impairments"—personal, external, and organizational. Generally, the standard requires that auditors decline engagements when impairments would affect the auditor's capability to perform work and report results impartially, and exhorts auditors to avoid situations that "could lead reasonable third parties with knowledge of the relevant facts and circumstances to conclude that the auditor is not able to maintain independence."[7] In those situations in which the government auditor cannot decline because of legislative or other requirements, the auditor must report those impairments. The standard also requires audit organizations to establish policies to identify, avoid, and where necessary, mitigate impairments.[8]

The most significant change in Amendment 3 relates to non-audit services. Auditors perform a variety of services, including audit and non-audit services. Non-audit services need not comply with the *Yellow Book*, and are often referred to as management advisory services. Non-audit services include gathering or explaining information and providing technical advice. Often, these services also involve gathering questions for a hearing, preparing reports from unverified or verified data, developing audit methods and plans, and providing advice concerning information systems and controls. Non-audit services differ from audit services in that they either directly support an entity's operations, such as processing payroll or developing internal controls, or do not involve the verification or evaluation of management-provided data. The concern addressed by Amendment 3 is that non-audit engagements might impair an

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1. Among its responsibilities, the GAO establishes auditing and accounting standards and principles for the U.S. Government. *See* Office of Federal Procurement Policy Act, 41 U.S.C. § 422 (2000).

2. In January 2002, the GAO issued its "exposure draft" of the revised *Yellow Book* for comment, and explained that the draft revision was intended, among other things, to strengthen and streamline standards This draft did not include the independence standard, however, which the GAO was revising separately. The comment period closed in April 2002. According to the GAO's Web site, the revised *Yellow Book* will issue in early 2003. *See* GAO Presentation, AICPA National Governmental Accounting and Auditing Update Conference, Washington, D.C., "What Will Change in the New Yellow Book, GAO-02-1081SP" (Aug. 2002), *available at* http://www.gao.gov/govaud/gao021081sp.pdf.

3. Press Statement, General Accounting Office (July 2, 2002) [hereinafter GAO Press Statement], *available at* http://www.gao.gov/govaud/pressreleaseqa.pdf. Underscoring this link between audit standards and recent accounting scandals, the Comptroller General also explained:

> One issue that has recently been in the press is the largely unexpected bankruptcy of one of the United States' largest corporations, Enron Corporation. A few bad actors who do bad things can have catastrophic consequences for many innocent people. With regard to the Enron situation, it seems pretty clear that a number of players failed to properly discharge their respective responsibilities. These breaches of trust have sent a shock wave through the accountability profession and the investor community.

Hon. David M. Walker, Comptroller General of the United States, Address at the Fourteenth Biennial Forum of Government Auditors, Providence, Rhode Island, "The Role of GAO and Other Government Auditors in the 21st Century" (May 20, 2002) [hereinafter Walker Address], *available at* http://www.gao.gov/cghome/14thbf.html.

4. *See* U.S. Dep't. of Defense, Contract Audit Agency Manual 7640.1, DCAA Contract Audit Manual ch. 2 (1 Jan. 2001) [hereinafter CAM].

5. Section 4 of the Inspector General Act of 1978 requires that federally appointed inspectors general observe the Comptroller General's standards when auditing federal organizations and functions. 5 U.S.C. app. § 3 (2000) (as amended).

6. Gen. Acct. Off., Rep. No. 02-388G, *Government Auditing Standards, Amendment No. 3, Independence* (Jan. 25, 2002) [hereinafter *Amendment 3*].

7. *Id.* at 1.

8. *Id.*

audit organization's independence if it becomes necessary to audit data or systems created, designed, or administered pursuant to a non-audit engagement in which the organization participated.[9]

To avoid these "impairments" to independence, Amendment 3 provides a principle-based threshold test, supplemented with a few safeguards.[10] The new standard is based on two overarching principles: (1) auditors should not perform management functions or make management decisions; and (2) auditors should not audit their own work or provide non-audit services in situations where the amounts or services involved are significant or material to the subject matter of the audit.[11] If an auditor or audit organization cannot be certain that a proposed engagement passes that test, the auditor or organization may not accept the engagement. If the engagement passes this principles test, certain supplemental safeguards, designed to ensure that there is no conflict or misunderstanding arising out of the non-audit engagement, must also be observed.[12]

The new standard expressly prohibits auditors from providing certain bookkeeping or record-keeping services, and limits payroll processing and certain other services, all of which are presently permitted under auditing standards of the American Institute of Certified Public Accountants (AICPA).[13] At the same time, the standard permits auditors to provide routine advice and answer technical questions without violating the two overarching principles or having to meet the supplemental safeguards. The standard also provides examples of how certain services would be treated under the new rules.[14]

Following the issuance of Amendment 3, a host of questions arose concerning its timing and implementation. The GAO considered these questions to be so substantial that it extended Amendment 3's effective date from 1 October 2002 to 1 January 2003. Similarly, the GAO grandfathered any non-audit services that were initiated, agreed to, or performed by 30 June 2002, provided that the non-audit services were completed by 30 June 2003.

In July 2002, the GAO gave a lengthy response to these questions.[15] The questions and answers concerned the sort of practical details that only an auditor or his lawyer would appreciate, but also addressed the concepts underlying the amendment. The practical details underscored the amendment's burdens and concerned such thorny issues as whether an organization's independence would be impaired by completing non-audit work even shortly after the June 2003 deadline. Reflecting the seriousness with which the GAO views this matter, the guidance explained that even if an audit organization took until July 2003 to complete a non-audit service engagement (for example, implementing a client's accounting system), the audit organization would be precluded from performing an audit of the client's financial statement (unless, for example, the accounting system was subsequently redesigned).[16] In addition to addressing these practical details, the GAO addressed the concepts underlying the new rules, discussing questions such as what constitutes a "management function," the meaning of "significance/materiality," and the scope of the impairment.[17] Generally, the guidance provides that an auditor must examine the "totality of the circumstances" in determining whether any non-audit work impairs the auditor's independence.[18]

According to the Comptroller General, this amendment is the first of several planned steps in connection with non-audit services covered by the *Yellow Book*. Specifically, the Comptroller General has stated that he plans to work with the Federal Accounting Standards Advisory Board, which develops generally accepted accounting principles for the federal government, to determine what type of additional disclosures relating to non-audit services may be appropriate. He has also suggested that the AICPA "raise its independence standards to those contained in this new standard in order to eliminate any inconsistency between this standard and their current standards."[19] The Comptroller General also has asked his Advisory Council on

9. *Id*. at 6.

10. The Comptroller General has described Amendment 3 as employing "a principles-based approach instead of a rules-based approach." Walker Address, *supra* note 3.

11. *Amendment 3*, *supra* note 6, at 7.

12. *Id*. at 9.

13. *Id*. at 2.

14. *Id*. at 8.

15. GEN. ACT. OFF., REP. NO. 02-870G, *Government Auditing Standards, Answers to Independence Standard Questions* (July 2, 2002).

16. *Id*. at 6-7.

17. *Id*. at 11.

18. *Id*. at 20.

19. GAO Press Statement, *supra* note 3.

Government Auditing Standards to review and monitor this area to determine what, if any, additional steps may be appropriate. Although many of these changes would not appear to affect the average government contract audit, practitioners must be aware of the core principles under which auditors operate to ensure that their work product is not compromised. Moreover, because the DCAA now offers a plethora of management advisory services, the new standard and its guidance will require considerable study.[20] Colonel Gillingham.

20. *See generally* CAM, *supra* note 4, ch. 15.

Nonappropriated Funds (NAF) Contracting

Pizza! Pizza!

In *Pacrim Pizza Co. v. Secretary of the Navy*,[1] a Marine Corps Morale, Welfare, and Recreation (MWR) non-appropriated fund instrumentality (NAFI) awarded a fast food services contract to the plaintiff, Pacrim. After the contracting officer terminated the contract for default, Pacrim appealed the decision to the Armed Services Board of Contract Appeals (ASBCA). The ASBCA sustained the termination, and Pacrim appealed to the U.S. Court of Appeals for the Federal Circuit (CAFC), pursuant to a clause in the contract declaring that the CAFC had jurisdiction under the Contract Disputes Act (CDA).[2] The CAFC acknowledged that it had jurisdiction over appeals from agency boards of contract appeals when the Contract Disputes Act (CDA) applied.[3] The CDA itself, however, limits the court's jurisdiction to covered NAFI contracts of the armed forces exchanges; therefore, the CAFC held that the non-appropriated funds doctrine deprived it of jurisdiction.[4] As the court stated, "A NAFI may be a covered contracting entity under the Contract Disputes Act if it is closely affiliated with a post exchange and meets a three part test."[5] The court held that the contract failed to meet the "threshold requirement that the NAFI be closely affiliated with a post exchange."[6] The contract's declaration of jurisdiction was not controlling. The CAFC found that "only Congress can grant waivers of sovereign immunity; parties may not by contract bestow jurisdiction on a court."[7] The CAFC dismissed the appeal, holding that the enumerated exchange exceptions excluded the MWR entity.[8]

AAFES, Yes; Other-Than-Contract Claims, No.

The CAFC recently affirmed the U.S. Court of Federal Claims (COFC) in *Taylor v. United States*,[9] holding that the court lacked jurisdiction over a suit by former employees of the Army and Air Force Exchange Services (AAFES). In *Taylor*, the plaintiffs retired early from AAFES during the 1990 military drawdown. The plaintiffs argued that a statute authorized the use of appropriated funds for NAFI separation pay. At the time, 5 U.S.C. § 5597 authorized the Secretary of Defense to pay a voluntary separation incentive of up to $25,000 "to encourage eligible employees to separate from the service voluntarily."[10] AAFES refused to pay the separation pay. The plaintiffs sued, alleging that 5 U.S.C. § 5597 waived sovereign immunity.[11]

While "Congress amended the Tucker Act[12] to authorize contract claims against AAFES and certain other NAFIs, the

1. 304 F.3d 1291 (Fed. Cir. 2002).

2. *Id*. at 1292. The Navy alleged that Pacrim failed to comply with the accounting and discrimination provisions of the contract and the equal employment opportunities clause in the contract. *Id*.

3. *Id*. The CAFC has jurisdiction over appeals from final decisions of agency boards of contract appeals. 28 U.S.C. § 1295(a)(10) (2000).

4. *Pacrim*, 304 F.3d at 1292-93; *see* 28 U.S.C. §§ 1346(a)(2), 1491(a)(1) (limiting coverage of NAFI contracts to express or implied contracts with the Army and Air Force Exchange Service, Navy Exchanges, Marine Corps Exchanges, Coast Guard Exchanges, or Exchange Councils of the National Aeronautics and Space Administration). "The general rule is that the Court of Federal Claims lacks jurisdiction to grant judgment against the United States on a claim against a NAFI because the United States has not assumed the financial obligations of those entities by appropriating funds to them." Taylor v. United States, 303 F.3d 1357, 1361 (2002).

5. *Pacrim*, 304 F.3d at 1292-93. The three part test is: "[I]t must have sufficient assets to reimburse the United States the cost of a judgment, be clearly defined as within the resale system, and provide financial data sufficient to predict the governments potential liability." McDonald's Corp. v. United States, 926 F.2d 1126 (Fed. Cir. 1991).

6. *Pacrim*, 304 F.3d at 1293. The court held that the three-part test did not apply until the facts of the case met the threshold requirement. *Id.*

7. *Id*. at 1294.

8. *Id*.

9. 303 F.3d. 1357 (Fed. Cir. 2002).

10. *Id*. at 1359.

11. *Id.* at 1360. The plaintiffs originally filed suit in the U.S. District Court for the Northern District of Texas. The district court "determined COFC had exclusive jurisdiction over the retirees' section 5597 claim under the Tucker Act because the retirees sought more than $10,000." *Id.* at 1359. The COFC determined that it lacked jurisdiction and dismissed. The retirees appealed. *Id.*

12. 28 U.S.C. § 1491(a)(1) (2000). The court stated:

> The jurisdictional grant in the Tucker Act is limited by the requirement that judgments awarded by the Court of Federal Claims must be paid out of appropriated funds. Hence, the Tucker Act generally does not provide the Court of Federal Claims with jurisdiction over claims against NAFIs such as AAFES.

Taylor, 303 F.3d at 1360.

plaintiffs acknowledged their claim was not based in contract."[13] Absent an express statute waiving sovereign immunity, the CAFC affirmed the COFC's holding that it lacked jurisdiction.[14] The CAFC held that "§ 5597 did not expressly extend to the NAFI employees."[15] The court also stated that although a Department of Defense (DOD) memo later authorized "NAFI separation payments from appropriated funds, . . . without express congressional authorization, the DOD memo was irrelevant to the jurisdictional issue because only an express statute may waive the sovereign immunity of the United States."[16] The CAFC affirmed the COFC's dismissal.[17]

UNICOR Is a NAFI

Last year, the CAFC affirmed a COFC holding that it lacked jurisdiction over a self-funding government agency.[18] This year, in *Aaron v. United States*,[19] the COFC held that Federal Prison Industries, Inc. (UNICOR) is a NAFI, and that the court therefore lacked jurisdiction over claims against UNICOR. In *Taylor*, UNICOR employees alleged that UNICOR violated the Federal Employees Pay Act[20] (FEPA) by failing to pay overtime for pre-shift and post-shift activities.[21] The COFC held that UNICOR is a NAFI and that the "[c]ourt's jurisdiction under the Tucker Act[22] must be confined to cases in which appropriated funds can be obligated."[23] The COFC found that Congress clearly intended to keep the financial obligations of UNICOR separate from the general treasury.

The COFC concluded it that lacked jurisdiction under the Tucker Act because the non-appropriated fund exception applied.[24] The court dismissed the plaintiffs' appeal because no express language in the FEPA waived the bar of sovereign immunity.[25]

The COFC reiterated that UNICOR is a NAFI in *Core Concepts of Florida, Inc. v. United States*.[26] In *Core Concepts*, UNICOR terminated the plaintiff's requirements contract.[27] The government moved to dismiss the plaintiff's claim, based on the ruling in *Aaron*.[28] The COFC reviewed the relevant statutes and their legislative history, and concluded that Congress "decreed that UNICOR's operation employs funds derived from the sale of products or byproducts by UNICOR or services of federal prisoners."[29] The COFC held that it lacked jurisdiction and granted the government's motion to dismiss.[30]

13. *Taylor*, 303 F.3d at 1360.

14. *Id*. In 1999, the CAFC ruled that the COFC had jurisdiction over the claim of a NAFI employee who sued under the Fair Labor Standards Act, 29 U.S.C. § 207(a)(1) (2000), because the Act contained a wavier of sovereign immunity. El-Sheikh v. United States, 177 F.3d 1321 (Fed. Cir. 1999); *see also* Major Louis A. Chiarella et al., *Contract and Fiscal Law Developments of 2000—The Year in Review*, ARMY LAW., Jan. 2001, at 43 [hereinafter *2000 Year in Review*].

15. *Taylor*, 303 F.3d at 1361.

16. *Id*.

17. *Id*.

18. *See* Major John J. Siemietkowski et al., *Contract and Fiscal Law Developments of 2002—The Year in Review*, ARMY LAW., Jan./Feb. 2002, at 138 [hereinafter *2002 Year in Review*]; Furash & Co. v. United States, 252 F.3d 1336 (Fed. Cir 2001). *Furash* involved the U.S. Finance Board, an independent government agency supported by assessments on member banks rather than by appropriated funds. *Id.*

19. 51 Fed. Cl. 690 (2002). The plaintiffs were employees or former employees of Federal Prison Industries, Inc., also known as UNICOR. *Id.* at 690-91.

20. 5 U.S.C. §§ 5542, 5544 (2000).

21. *Aaron*, 51 Fed. Cl. at 690-91. "The plaintiffs also alleged UNICOR violated the Fair Labor Standards Act, . . . but agreed at oral arguments that only FEPA claims were at issue." *Id.*

22. 28 U.S.C. § 1491(a)(1) (2000).

23. *Aaron*, 51 Fed. Cl. at 691.

24. *Id*. at 694.

25. *Id*. at 695.

26. No. 00-3080C (Ct. Fed. Cl. Aug. 23, 2002) (unpublished), *available at* http://www.contracts.ogc.doc.gov/cld/cofcdec.html#cofc.

27. *Id*. at 1.

28. *Aaron*, 51 Fed. Cl. 690 (2002).

29. *Core Concepts*, No. 00-3080C, at 2.

30. *Id*.

Federal Retirement Thrift Investment Board Is Not a NAFI

In *American Management Systems, Inc. v. United States*,[31] the COFC held that the Federal Retirement Thrift Investment Board (Thrift Board) is not a NAFI.[32] In 1997, the Thrift Board awarded a $30 million contract to American Management Systems (AMS) to design, develop, and implement an automated record-keeping system. The Thrift Board terminated the contract after numerous delays and substantial cost increases. When AMS challenged the termination, the Thrift Board moved to dismiss.[33] The Thrift Board asserted that it was a NAFI, arguing that it does not receive any appropriations, and that it pays its expenses from private funds. The COFC disagreed, finding that the Thrift Board receives appropriated funds and therefore is not a NAFI.[34]

The court found that 5 U.S.C. § 8437(c) specifically provides that "the sums in the Thrift Savings Fund are appropriated and shall remain available without fiscal year limitation to pay administrative expenses of the Federal Retirement Thrift Investment Management System."[35] While the statute identified contributions and net earnings to be held in trust for the employees, the COFC held that the statute subjected the funds to a condition to pay the expenses of the Thrift Board. The court determined that the condition "attaches to those funds at the instant of their appropriation by Congress."[36] The court also noted that the Thrift Board was required to prepare an annual budget that, if approved, would be made part of the federal budget, and which would be subject to congressional review.[37] The COFC concluded that the "Thrift Board is a governmental agency whose administrative expenses are payable out of public funds made available through a congressional appropriation" and denied the government's motion to dismiss.[38]
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31. 53 Fed. Cl. 525 (2002).

32. *Id.* at 529. "The Thrift Board is responsible for managing the assets of the Thrift Savings Fund, a tax-deferred saving account created under the Federal Employees' Retirement System Act. The Board manages funds for federal employees and members of the uniformed services." *Id.* at 525-26.

33. *Id.* at 526.

34. *Id.* at 526-27. Specifically, the defendants argued that 5 U.S.C. §§ 8437(d) and (e)(1) "taken together demonstrate that the Thrift Board is not granted any appropriations of its own. Instead, the Thrift Board is required to draw its funding from monies that originate as appropriations granted to employer agencies for the payment of contributions on behalf of their employees." *Id.* at 527; *see* 5 U.S.C. §§ 8351, 8401-8479 (codifying the Federal Employees Retirement System).

35. *Am. Mgmt. Sys.*, 53 Fed. Cl. at 527.

36. *Id.*

37. *Id.* at 528.

38. *Id.* at 529.